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a guide
for the

MUNICIPAL AUDITOR

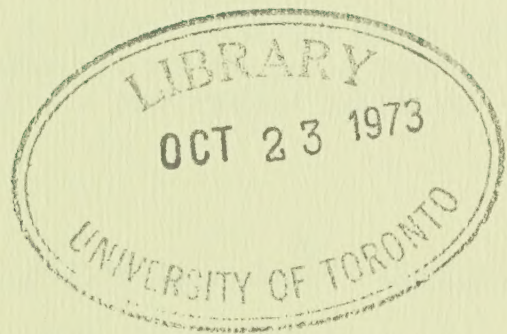
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a guide for the **MUNICIPAL AUDITOR** in ontario



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Deputy Minister: W. H. Palmer


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The Institute of Chartered Accountants of Ontario

June 5, 1970

Here is a book that fills a long-felt gap in the literature of our profession. Produced by the Department of Municipal Affairs of Ontario, the book follows and complements the recent important changes in financial reporting developed by the Department for Ontario municipalities.

The Department of Municipal Affairs is to be commended for its initiative in making these changes, in getting the book under way, and for pressing forward to further work in these areas.

During the past five years our Committee has worked closely with members of the Department in the development of these projects, and we share with the Department's members a sense of accomplishment in progress to date.

There is a minimum required body of knowledge which every municipal auditor must possess - 'A Guide for the Municipal Auditor in Ontario' outlines these requirements.

We wholeheartedly endorse the contents of the book, and recommend it to all Chartered Accountants who are currently engaged by municipal clients, or who contemplate taking on such engagements.

W.M. Brace, F.C.A.

Chairman

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INTRODUCTION

In principle the audit of a municipality differs little from that of a business corporation. In detail, however, there are important differences. This book describes those differences and explains why they exist. It has been written with the newly-appointed or potential municipal auditor in mind; it bridges the gap between business and municipal audits — an area where there has been little research to date.

At the same time, we want to establish what duties “an auditor shall perform . . . as are prescribed by the Department”; this book replaces our detailed instructions issued previously. As an auditor you are professionally competent to decide what audit tests are necessary in various circumstances. So — except where specifically noted — your duties and responsibilities as a municipal auditor are the same as for any other audit.

We want to show how it is imperative for you to acquire a full working knowledge of municipal operations, accounting and legislation when you undertake a municipal audit. Once you have acquired this working knowledge, you will then be able to render a high level of service to local government.

You will find little here about the preparation of financial statements or the generally accepted accounting principles applicable to municipalities. This information is in the *Municipal Finance Manual* issued by the Department. .

As you will come to realize, the municipal accountability pattern is anything but simple; few people outside municipal government fully comprehend it. Moreover there is every prospect that complexities in municipal accounting will increase in the future. The need is going to increase in the coming years for a professional auditor who can both safeguard the integrity of the system and provide constructive services aimed at improving the financial administration of a municipality.

We are well aware that municipalities — like every other human institution — are less than ideal. But we thought that rather than dwell on what goes wrong in local government from the auditor’s point of view, we could provide a yardstick by which you can judge the operations of your clients. Consequently the ideal municipality we use as an example in this book is imaginary: it possesses all the qualities which you will consider necessary and desirable. For example, it is large enough to achieve a thoroughly efficient operation, but is still not necessarily “big”. It is well administered: the appointed officials are experts in their own field and the elected representatives function well within their policy making sphere. It has a good system of internal control. Individual responsibilities have been clearly assigned with an adequate division of duties, satisfactory accounting records and sound operating procedures.

We have limited our scope to the audit of a municipal corporation. But within the responsibilities of your audit of a municipality you will be required to audit several other bodies: public utility commissions, library boards, joint boards and so on. The audit of these bodies is not covered in this book, and there are no references to the audit of school boards. Hopefully, a booklet on the subject of auditing local boards will be published sometime soon.

This book is the outcome of an extensive study of municipal auditing initiated by Mr. Paul Hickey, F.C.A., Assistant Deputy Minister of the Department of Municipal Affairs. This study was conducted by the staff of the Department's Municipal Accounting Branch with the assistance of Mr. B. F. Toney, C.A., of Touche Ross & Co. Mr. E. J. Reynolds, C.A., Manager of Accounting Research requires special mention for the enthusiasm and professional skill he contributed to the project. Many municipal auditors in Ontario supplied much of the information, and made many helpful and constructive suggestions. In particular, thanks are due to Mr. W. M. Brace, F.C.A., of Touche, Ross & Co., the chairman of the Ontario Institute's Municipal Accounting and Auditing Committee, and to Mr. D. W. Scully, F.C.A., of Clarkson, Gordon & Co., and Mr. B. R. Waters, C.A., of Deloitte, Plender, Haskins and Sells, who made many improvements to the original manuscript.

One of the most satisfying circumstances connected with the publication of this book is its endorsement by the Municipal Accounting and Auditing Committee of the Institute of Chartered Accountants of Ontario.

A. W. Reeve
Directing of Municipal Accounting
Department of Municipal Affairs

June, 1970

THE ONTARIO MUNICIPALITY

The municipality as a corporate entity

Legal definition

According to *The Municipal Act*, “municipality means a locality the inhabitants of which are incorporated.”

Very succinct. But, beyond telling us that a municipality is a geographic area made up of people, not too helpful.

The Canadian Encyclopedic Digest, which is a compendium of statute and case law, supplies a more useful definition:

“A body corporate constituted by the incorporation of the inhabitants, residing within a defined area, upon whom the Legislature has, either directly or through some intermediate agency, conferred corporate status, rights and liabilities, including the right to administer through the agency of an elected council, or other governing body, such matters of local concern as are either expressly specified, or are as necessarily implied from the nature and extent of the authority conferred.”

So a municipality is a corporation. In many ways it is similar to a business corporation incorporated under *The Corporations Act*: it has legal personality and status. It can sue and be sued, make contracts and borrow money. Its existence and its rights and duties are separate from those of its constituents.

To a point, the structure of a municipality is also like that of a business corporation. Its members elect a council to manage the corporation and to take all executive action on its behalf — just as the shareholders of a business corporation elect a board of directors to manage its affairs. The municipal council appoints officials to carry out its day-to-day operations — just as a board of directors appoints company officers.

We need not dwell on the parallels between business and municipal corporations — they will be obvious to you. Far more interesting and important are the differences between the two types of corporation.

For example, consider the relationship of a municipal corporation with its members — which is not fully comparable to that of a business corporation with its shareholders. Or, examine the role of appointed officials; in a municipal corporation, a person can never be both an elected member of the council and an appointed official at one and the same time. And the responsibility and authority of an elected municipal council are comparatively restricted.

Moreover, a business corporation sets out with the avowed goal of earning a profit. Not so the municipal corporation. A municipality is incorporated in order to provide a range of services for its constituents — at the lowest possible cost to the constituents. Service, not profit, is the purpose of the municipal corporation.

With, perhaps, the exception of the largest conglomerates, no business corporation has such a wide variety of operations as that found in an Ontario municipal corporation. Police and fire protection, bridge and road building, sewage and garbage disposal, parks and recreational facilities, community planning and zoning control, libraries and preventative health care, homes for the aged and financial help for the needy — all are numbered among the responsibilities of a modern urban municipal corporation.

As a result, municipal corporations tend to be highly complex organizations, administered by many different departments, committees and boards. Both elected representatives and appointed officials find their time is cut out just trying to keep up with the progress of every facet of the operation for which they are responsible.

When you compare the operations of a municipality to those of the provincial and federal governments you will find one major difference. In a municipality there is no cabinet made up of elected members of political party. The elected representatives of a municipal council vary greatly in personality, ambition and interests — and since they are seldom elected as a team or party, it is difficult for them to act as a team.

Relationship with constituents

To understand your client's operation, you need to comprehend the relationship which exists between a municipi-

ality and its constituents: inhabitants, ratepayers and electors. This relationship is reflected in the wording of the salutation of the auditor's report. (See page 28).

- (a) *Inhabitants* are all the people who live within the geographical boundaries of a municipality. Remember, a municipality is a *locality, the inhabitants of which are incorporated*.
- (b) *Ratepayers* are people who pay either business or property taxes to the municipal corporation. Therefore, all property owners and business tenants are ratepayers — whether they live there or not.
- (c) *Electors* are those inhabitants and ratepayers who are entitled to vote at municipal elections. Some municipalities allow only *ratepayers* who are 21 or over to vote. Other municipalities, however, have adopted the provisions of *The Municipal Franchise Extension Act*, and also permit all *inhabitants* of 21 and over to vote (regardless of whether or not they are ratepayers).

It is important to realize that the council of a municipality is elected both to legislate and to administer the municipality on behalf of the members of the corporation: the *inhabitants*. *Ratepayers* supply the money needed to operate the municipality, but it should be the *inhabitants* who command the attention of the council. The elected represen-



... inhabitants are the people who live within the geographical boundaries of a municipality ...

... ratepayers are people who pay either business or property taxes to the municipal corporation ...

... electors are those inhabitants and ratepayers who are entitled to vote at municipal elections ...

tatives are accountable to the *inhabitants* of a municipality. Your role in this accountability pattern is explained later in this book.

Part of the accountability concept involves impartiality. A municipality must treat all its constituents impartially; and consideration for this principle has led to much of the legislation affecting municipalities — such as that dealing with conflict of interest and that providing for the appeal of assessment.

Grasp the importance of impartiality in local government, and you will appreciate why many apparently cumbersome administrative procedures are required by law. The Legislature wishes to ensure that the rights of every individual constituent of a municipality are being protected. For example, all real property must be assessed and the council must levy taxes on the whole assessment each year — failure to do so would be to show partiality to certain constituents. One of the greatest causes of friction between a municipality and its constituents is the showing of real or imagined favouritism. Deliberate partiality on the part of elected representatives or appointed officials is reprehensible, but sometimes a municipal council or a local board will discriminate unwittingly by changing an established policy or procedure. Incidentally, when you advise a municipality on methods of improving its operations, bear in mind this question of impartiality.

Types of municipality

In Ontario, there are eight distinct types of municipality:

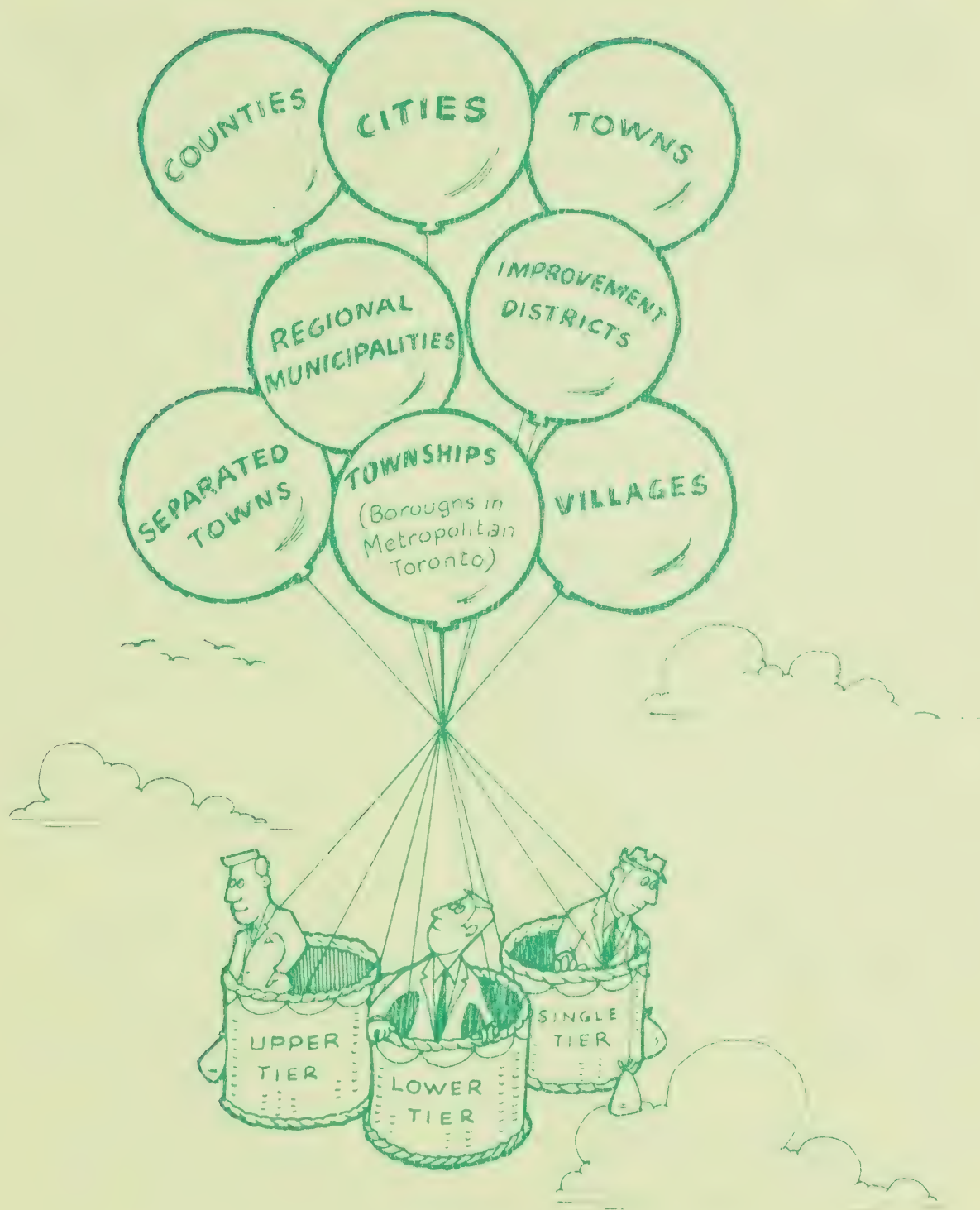
- Cities
- Counties
- Improvement districts
- Regional municipalities
- Separated towns
- Towns
- Townships (called “boroughs” in Metropolitan Toronto)
- Villages

Types of municipalities were distinguished, traditionally, by their size of population and their rural or urban nature. Today, however, the growth of population and the spread of urban development into previously rural areas have blurred traditional distinctions. Moreover, the structure of local government is presently undergoing radical change — resulting in the creation of new metropolitan and regional municipalities.

A more meaningful contemporary distinction between types of municipality is by tiers. A municipality is either upper tier, lower tier or single tier. The range of services which a municipality renders its constituents depends not upon its title, but upon its tier position.

Double tier systems

The whole of southern Ontario is organized into municipalities; there are no unorganized areas of land. In the traditional double tier system, the county is the upper tier and the improvement districts, towns, townships and



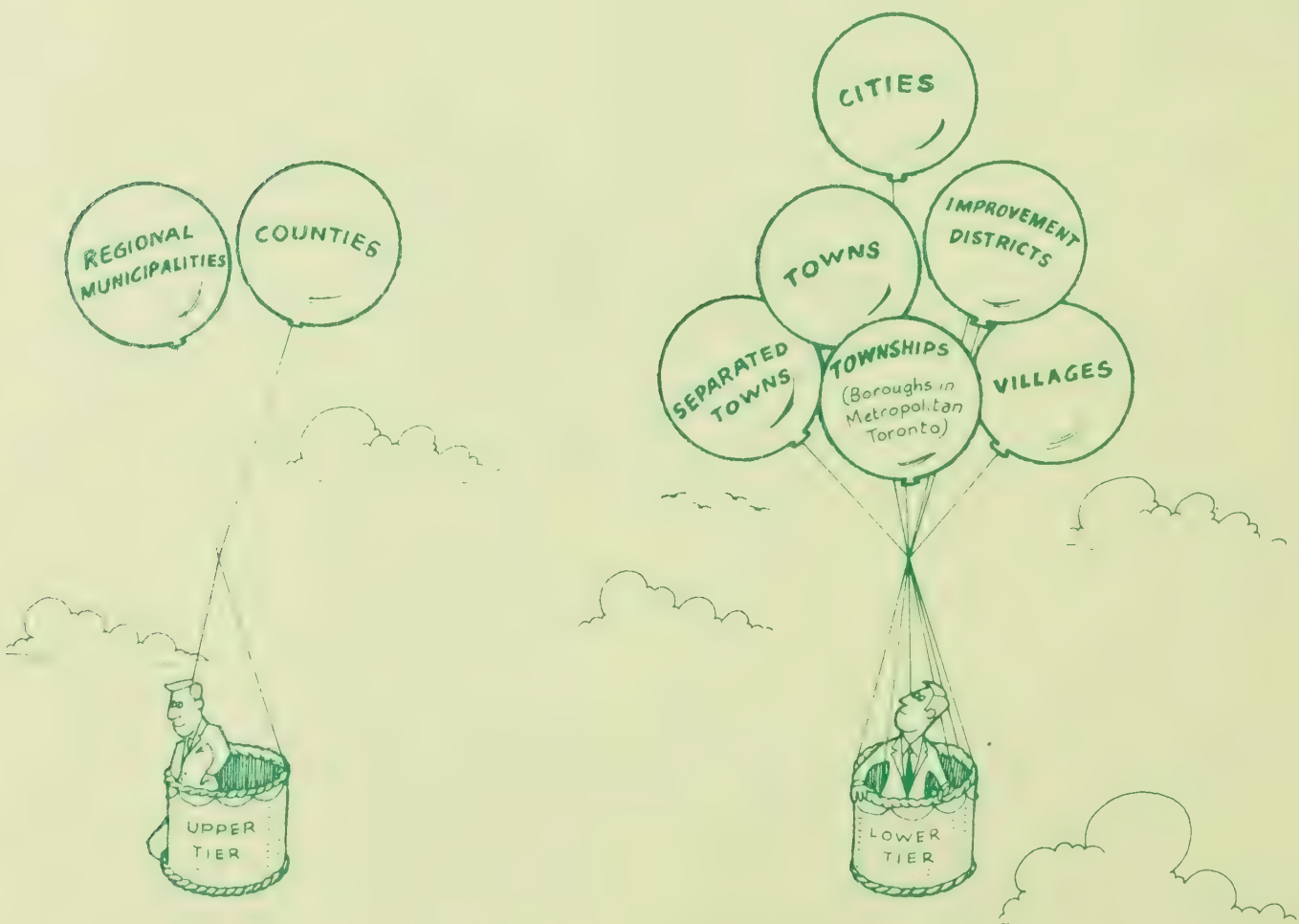
... in Ontario, there are eight distinct types of municipality ...

... a municipality is either upper tier, lower tier or single tier ...

villages (but not the cities or separated towns) within its borders are the lower tier.

The reeves and deputy reeves of lower tier municipalities sit ex-officio (by reason of their office) as members of the county council. A county does not levy taxes directly, but apportions its costs to the lower tier municipalities. Counties are responsible for the county road system and often for social services, such as aid for the needy, preventative health services, homes for the aged and libraries. Not all counties provide these services; in some counties the lower tier municipalities continue to provide them to their own inhabitants.

More recently, metropolitan and regional municipalities have provided another form of double tier structure. All the municipalities within a regional or metropolitan municipality are the lower tier — no matter what their titles may be — and the regional or metropolitan municipality forms the upper tier. Members of regional or metropolitan councils sit either ex-officio (as in the case of county councillors) or are elected by general vote in the lower tier municipalities. Regional and metropolitan municipalities do not tax directly, but like a county, apportion their costs to the lower tier municipalities. But metropolitan and regional municipalities provide far more services than do counties. Roads, social services,



water treatment, sewage treatment, regional planning, police protection and long term financing are all metropolitan and regional services. Lower tier municipalities are responsible for local roadways, water distribution, garbage and sewage collection, local planning and similar functions.

Single tier systems

Single tier municipalities occur throughout northern Ontario and in some places in southern Ontario. In northern Ontario, most municipalities are separated from one another by unorganized areas; in the south, cities and separated towns which are outside regional or metropolitan municipalities are single tier. Single tier municipalities raise their own revenue and supply their own services; but they may (if they see fit) co-operate with neighbouring

municipalities to provide services through joint boards (see page 20). Examples of such co-operation are found in county or district social and family service units, suburban road commissions, and so on.

You should be aware of the division of responsibility for services — which depends on whether your client is a single tier, upper tier or lower tier municipality.

Improvement districts

Among municipalities there is a unique type: the improvement district. In places where there has been sudden growth and where no basic community existed before an industry — such as a mine or a pulp and paper plant — moved in, an improvement district provides quick municipal organization. A board of trustees manages the municipality until the resident ratepayers want to establish a town or a township. Most improvement districts are located in northern Ontario.

Local ethos

From what we have said so far, you will have realized that every generalization applied to Ontario local government is capable of exception. Each municipal corporation is, to some extent, a unique entity. You may find this fact an irritation if you are trying to learn something about municipalities in general, but there is good reason for it. If local government is to operate efficiently, it must adapt itself to meet the demands of local conditions. Each municipality therefore practices self-government



on a wide range of specified matters; each attempts to provide good government to its own peculiar area.

There are, in fact, two opposing forces at work upon the local nature of each municipality: influences tending to produce uniformity among all municipalities, and tendencies which encourage diversity.

Three major influences which induce municipal uniformity are: legislation, court decisions and the promotion of basic service standards by the Province.

Almost all municipalities owe their existence to an Act of the Legislature. Most were created under the provisions of *The Municipal Act*, which is sometimes supplemented by private acts. Metropolitan and regional municipalities were each specially created by a separate act — *The Municipality of Metropolitan Toronto Act*, *The Regional Municipality of Ottawa-Carleton Act* and so on. Some municipalities owe their existence to the colonial administration which preceded the Province of Ontario. Toronto, Kingston and Brockville are examples. But with few exceptions, the provisions of *The Municipal Act* and other pieces of general legislation apply to all municipalities alike. For this reason, court decisions which interpret municipal law relate to all municipalities.

The Province encourages municipalities to provide certain basic services by:

- programs which provide grants based

on actual expenditure (such as grants for highways).

- capital grants for needed facilities. These grants take the form of either capital donations or reimbursement of debt charges. (Examples are grants for constructing community centres and for reimbursing the debt charges on schools).
- grants for the salary of certain appointed officials. These grants are made if a municipality hires a properly qualified official (such as a full time recreation officer).
- operating grants to joint boards. Such grants, which are larger in amount than grants to individual municipalities, encourage municipalities to co-operate and form larger units to service greater areas. (An example of such co-operative ventures is a health unit).
- grants towards the cost of planning and implementing unusually expensive programs (such as urban renewal schemes).
- penalties for failing to provide certain services. (The Ontario Water Resources Commission can bring a municipality before the courts if it refuses to provide for sewage treatment, for example).

In spite of these pressures, there is a strong tendency toward municipal individuality. The inhabitants of each municipality demand services which make it a comfortable, convenient

and interesting place in which to live and work. Naturally, such local pressures differ slightly in each area, causing one municipality to have a different order of priorities from another. *The Municipal Act* and other legislation recognizes this fact, and most of the statutory requirements affecting municipalities are permissive, not mandatory. There is, moreover, a great diversity of municipal structures; no two municipalities are identical. Each municipal corporation has developed its own unique organization of committees, departments, local boards and appointed officials. Each has allocated its own internal responsibilities and authority. In fact, different municipalities give different names to the same appointed official whose title and duties appear in *The Municipal Act*.

So whenever you find a generalization in this book, treat it with caution! Study your client's own organization and you will be able to apply to it what you learn here.

Relationship with the Province

In Canada, all political authority is divided between the federal and provincial governments. Municipalities are a concern of the provinces and not of the federal government simply because *The British North America Act* says so. Municipalities are not sovereign governments. They derive whatever powers they have from acts of the provincial legislature.

From time to time, municipal corporations find this limitation of power

frustrating. It may be necessary to carry out some needed local service which is not explicitly permitted in the existing legislation. Apart from acting outside its powers — in which case it risks challenge in the courts — a municipal council has to seek special provincial legislation giving it the authority to act.

There are three facets of the relationship between the Province and its municipalities: the responsibility for the provision of services for the citizens of Ontario, payment by the Province for some of the services supplied by local government, and the provincial direction and determination of municipal services.

Provincial and municipal services

The Legislature decides which services will be the responsibility of the provincial government and which the responsibility of local government. There are changes from local to provincial level and vice versa almost every year.

Financing arrangements for local services

Provincial revenues are widely used to defray the cost of certain municipal services. For example, the Department of Social and Family Services contributes to local social service departments and to homes for the aged. In all such cases, the actual service is rendered and administered by local government but the cost is paid substantially by the provincial government — in some cases the support

is 100% of the cost. Why does the Legislature require the Province to aid municipalities in this way? Three general answers can be given.

1. The provincial government could, of course, provide such services itself. But they are supplied more effectively if administration is kept at the local level and priorities are decided by local elected representatives.
2. The full range of services demanded of local government is too costly to be provided from municipal taxation.
3. The tax base of a municipality is inadequate to support the standard of service expected by most residents of Ontario. There is strong desire that the general quality of life should improve throughout the province even in areas where the ability of the local inhabitants to pay for it is severely limited.

Provincial direction and determination

Provincial government departments and agencies have close and direct ties with departments and boards of local government. The directive powers of the provincial government are extensive: some are used frequently but others are seldom, if ever, applied. To take a couple of contemporary and specific examples — the Ontario Municipal Board and the Ontario Water Resources Commission are both actively concerned in municipal activities.

The Ontario Municipal Board (OMB) is a partly administrative, partly judicial, body whose approval must be obtained by a municipality before it engages in certain activities such as incurring long term debt, or changing its zoning by-laws.

The Ontario Water Resources Commission (OWRC) is responsible for improving the quality of Ontario's water supply. It therefore requires municipalities to meet certain standards in supplying fresh water and in treating sewage.

On the other hand, the Department of Municipal Affairs (DMA) has wide directive powers which it seldom uses. Occasionally — when, for example, a municipality's solvency appears threatened, or its administration appears to be grossly inept or corrupt — the DMA may place a municipality under its supervision and control. Once matters have been placed on a sound footing, the administration is turned back to local control.

At first, you will probably be bewildered by the extent and variety of the relationships between your municipal client and the Province. As you come to understand municipal finance, you will see how provincial grants are involved in paying for locally administered services. And you will become fully aware of the effect your professional advice can have on your client's relationship with a provincial department or agency.

The pervasive influence of law

The important principle of *Ultra Vires*

The legal principle *Ultra Vires* is applied to municipal activities without exception. Put into plain English, *Ultra Vires* means that a corporation may do only those things that the statutes say it can do; it may not do anything for which it has no express authority.

The principle of *Ultra Vires* has almost passed out of use in business corporations. In the case of municipal corporations, however, the courts have insisted that *Ultra Vires* applies rigidly. There is good reason for this insistence. If municipalities were allowed to indulge in whatever they liked, they might do just that — and infringe on individual human rights. As matters stand, municipalities may engage in certain specified activities only; they have no legal authority to engage in other activities.

By way of illustration, a municipality may not agree to maintain an industry’s property assessment at a fixed level even if all its constituents want it — there is no legislation authorizing it to do so. Nor may it make a grant or contribution to a worthy cause (for example, a local service club) unless the legislation specifies the cause. A municipality may licence, regulate and tax — but only in the form and manner prescribed by an act of the Legislature.

The responsibility for making sure a municipality observes the principle of *Ultra Vires* rests with the inhabitants or ratepayers. They, or any other party, may take the matter to the courts and have an offending by-law declared invalid.

In order to determine whether or not the financial statements of a municipality present fairly its financial position, you will need a basic working knowledge of the authority possessed by your client. *Ultra Vires* transactions may give rise to substantial contingent liabilities. If they are not adequately disclosed in the financial statements, your opinion may not be unqualified. (See Page 31). You are always entitled to ask — and to receive an unequivocal reply to — the question “What authority do you have for this transaction?”

There is a section in *The Municipal Act* which appears, at first glance, to bestow on a municipality the authority to do almost anything.

“Every council may pass such by-laws and make such regulations . . . in matters not specifically provided for by this Act as may be deemed expedient. . . .”

However, court decisions have placed a narrow interpretation on this section. According to the judges, it does not extend the existing powers of a municipality and in practice it is not applicable.

Municipal powers — complexity of legislation

The legislation authorizing munici-

palties to act increases with every session of the Ontario Legislature. There are now well over 100 statutes which affect municipalities to some degree. In addition to the statutes, there are also countless regulations and instructions issued by provincial government departments and agencies under the provisions of the statutes.

As a further complication, the Legislature has passed special private acts which empower a municipality to do things which other municipalities cannot do under the general legislation. These acts are usually found in municipalities which have been faced with problems that are uncommon to most Ontario local governments.

The whole arrangement is complex and, to the uninitiated, extremely confusing. In order to have a thorough working knowledge of municipal law, it is necessary to make yourself familiar with the pertinent legislation and regulations; the bibliography at the end of this book lists some of the more common Acts of the Legislature which concern municipalities. A good general rule to follow is to look in the obvious place first. *The Municipal Act*, to which we have referred, is the act governing the general conduct of municipalities. Other Acts deal with specific matters and usually their title is a fair indication of their content. If any legislation appears obscure, your client's solicitor should be able to interpret its meaning for you. Members of the Municipal Accounting Branch of the Department of Municipal Affairs can provide information about municipal finance

legislation and can give you information about common practices — but they do not give legal opinions.

Because the law is so important to a municipal audit, your relationship with solicitors will be more critical than in a normal business audit. Municipal law is very complex and on occasion, you may have reason to think that the legal opinion obtained by your client should be substantiated. You may want to obtain a second opinion before deciding on your reaction to a questionable situation.

Fortunately, means are available which give you easy access to statutes and regulations. You should consider having a minimum library of municipal law in your office. The basic work is the codified *Revised Statutes of Ontario* (RSO). Every ten years, a team of legal experts reviews the existing legislation in Ontario and compiles the *Revised Statutes*. But it must not be thought that having the most recent RSO at hand means that you have the up-to-date law at your finger-tips; legislation is passed so frequently that even when a fresh RSO is issued, it is outdated. The statutes passed at each session of the Legislature are published in the annual *Statutes of Ontario*, and there is a service which supplies a more or less continuous up-dating to the most recent RSO — *The Ontario Statute Citor*. (Details on where to obtain this service are in the bibliography).

Each year, at the end of the current session of the Legislature, the Depart-

ment of Municipal Affairs issues a useful little booklet called *Summary of Legislation Affecting Municipalities*. While not so thorough-going as the *Citator*, it nevertheless brings you right up-to-date on the last session's activities in the municipal field.

In addition to the basic legal references in a municipal law library, you would be well advised to keep on hand a copy of Rogers' *Law of Canadian Municipal Corporations* and to subscribe to the *Ontario Gazette*. Details of these and other important references are also in the bibliography.

The exercise of the council's power

In order to be binding and valid, policy decisions of the council must be enacted as by-laws and recorded in the minutes of the council. In certain cases the provincial legislation authorizes the council to act by passing a resolution, but whenever the validity of resolutions has been challenged in the courts, the judges have said that only by-laws are recognized as legal and binding. This is the reason why you should expect to find a by-law to support every important decision of the council — for instance there should be a by-law for every decision to borrow money from the bank, to levy the taxes, to share costs on a joint project, to begin a capital project, to adopt a budget, to hire a senior official — and to appoint you as the municipal auditor!

Fund accounting

Before we leave the subject of the law's pervasive influence, a word about fund accounting. In municipal financial operations, as in the operation of most other non-profit organizations, money raised or supplied for a particular purpose cannot be used for any other purpose. Legal restrictions and contractual agreements prevent it from being diverted to any other use. Fund accounting is a technique which is used to show that money has been used for the purpose for which it was obtained.

The funds most commonly used in municipal accounting in Ontario are *Capital Fund*, *Reserve Fund*, *Trust Fund* and *Revenue Fund*.

The *Capital Fund* is used to account for all capital expenditure and the financing of capital expenditure. Among the sources of capital financing are long term borrowing, money contributed by senior governments to assist with capital projects, and money raised for capital expenditure through current taxation. In addition, the *Capital Fund* is used to account for any money that is borrowed by a municipality on behalf of a local board (such as public utility) which itself lacks long term borrowing powers.

A *Reserve Fund* is established to account for assets which have been segregated for a specific purpose, either voluntarily or

because of legal or contractual reasons. As an illustration: contractual agreements with subdivision developers under which the municipality has received money to provide for the installation of water and sewage services will give rise to Reserve Funds. Other Reserve Funds may result from a voluntary decision of a municipal council or one of its local boards to set aside money to finance a capital project.

A *Trust Fund* (or an *Endowment Fund*) occurs in municipalities for much the same reasons as it occurs in hospitals, universities or charitable organizations.

The *Revenue Fund* is used to account for all revenues and resources which are not otherwise accounted for separately. Revenues which are unrestricted in use, such as the general taxation revenue of a municipality, are found in the Revenue Fund. In addition, some revenues which are earmarked for specific uses but which are not usually segregated and separately accounted for, may be found there. Two examples of such revenues are: taxes raised by a municipality on behalf of a school board, and local improvement charges which are raised only from taxpayers in a specified area of a municipality.

There is a trend in Ontario municipal financial reporting to reduce the number of funds reported separately to the public. But neither the need to

maintain separate accounting records for each fund, nor the legal requirement to segregate the assets of some funds from other assets of the municipality is eliminated. You should ascertain the current practice by consulting your *Municipal Finance Manual*.

The “procedure by-law”

For our purposes, the term “procedure by-law” means the by-law or by-laws which incorporate all the policies of council — including not only the procedures for council meetings but also the whole administration of a municipality. The general content of a procedure by-law is explained in A. H. Marshall’s *Financial Administration in Local Government*. The author is one of the world’s leading authorities on local government finance and his philosophy has been accepted in Ontario and elsewhere.

Unfortunately, the practice of having a well-documented procedure by-law is still far from universal. In many municipalities the recording of the council’s policy decisions is fragmented; seldom are the many practices and resolutions of council assembled in one by-law. All municipalities have by-laws covering policy, however. Examples are: the by-laws which appoint the treasurer and other officials and outline some of their duties, and the by-laws outlining the responsibilities of each committee. As a municipal auditor, you cannot ignore policy decisions of the council; even if your client’s system of internal control is adequate, you should also make sure that it agrees

with the policies of council. As explained below, it is only the council who has the authority to decide policy. If you find this authority is being usurped by individual officers or representatives, you should report the fact to the council. It can then decide whether to change the system or to change its policy.

The municipal structure and accountability pattern

The council

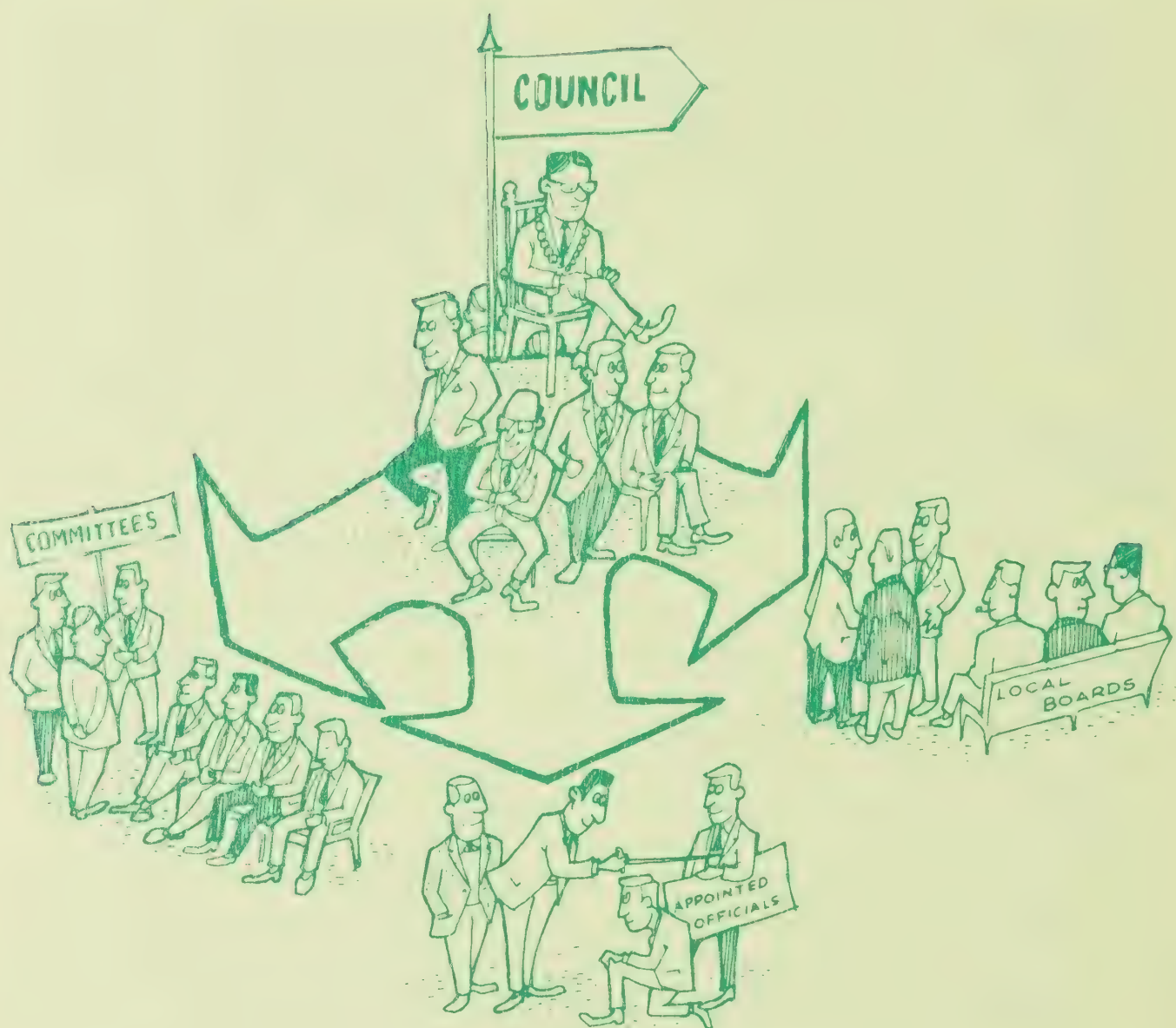
Properly speaking, nothing may take place in municipal operations unless the municipal council first gives its blessing. Policy is decided only by the council; appointed officials and elected representatives may advise and recommend certain courses of action, but the action is taken by the council. The council's authority is modified only by a degree of independence granted to some local boards by the statutes.

The council of a municipality has the central position in the accountability pattern. It both makes the policy and administers the municipal corporation on behalf of the inhabitants. Within a municipality, the council establishes the accountability pattern in its procedure by-law. The responsibilities and terms of reference for each committee are framed by the council. Senior officials are appointed by the council. Most local boards are established by the council and are accountable to the council for their actions.

In the provincial and federal governments the responsibility for legislation rests with the Legislature or Parliament, and the responsibility for administration rests with the Cabinet. But in local government, the council is both the legislator and the administrative executive. Naturally enough, the amount of administration in which council members will involve themselves varies with each municipality. In a small township or village, councillors normally keep a close eye on every activity; they appoint few officials. In a large city or regional government, most of the day-to-day details are delegated to the appointed officials by the procedure by-law.

It is the council which has authority to administer activities on behalf of the municipality; individual members of the council have no legal authority to act on behalf of the council or the municipality. The head of the council — the mayor, chairman, warden or reeve — may enjoy considerable influence and prestige, but he possesses very little real authority. He chairs meetings of the council and has the right to sit on all its committees, but his vote carries no more weight than any other member's vote. Authority invariably rests with the council as a whole.

There has been a great deal of discussion over the question of a council member's conflict of interest. This matter is impossible to define and therefore impossible to prevent by legislation. The law simply requires that any council member who has a relevant financial or subjective interest



... properly speaking, nothing may take place in municipal operations unless the municipal council first gives its blessing ...

... most of the detailed administrative work in which council members become involved is handled by committees ...

... the day to day details of municipal administration and advice on policy are the concern of appointed officials ...

... as the auditor of the municipality, you are automatically the auditor of all the local boards of the municipality — school boards are exceptions ...

in a matter under discussion shall declare that interest and shall refrain from discussion or voting on that matter.

Committees

Most of the detailed administrative work in which council members become involved is handled by committees. Because members of a committee become well versed in the activities for which they are responsible, they can develop positive recommendations for policy decisions more quickly. Generally, discussion is kept informal, and committee members have the opportunity to sound out local opinion before making a recommendation to the council. Incidentally, some municipal councils use the procedural device known as a “committee of the whole” to deal with complicated matters under discussion by the council. This device allows the entire council to dispense with formal rules of procedure to expedite the business. When the matter has been resolved, the council resumes its sitting and, if necessary, takes formal action.

The number of committees to be found in a municipality depends upon local needs, as does the membership of committees and the means of appointing chairmen and selecting committee members. *Standing committees* of the council are usually provided for such activities as public works, finance, fire protection and social and family services. *Special committees* are formed to handle one specific matter only, and sometimes include as members selected experts who are

not members of the council. Standing committees generally continue during the lifetime of the council. A special committee, having a more limited purpose, usually disbands when its task has been accomplished.

Generally, committees of the council are not recognized by provincial legislation, so their function is restricted to that of advising or recommending. Before a committee resolution becomes effective, it must be passed by the council in the form of a by-law. Nevertheless, in spite of the fact that they have no legal status, committees of the council can have a strong influence in a municipality. You will find their specific responsibilities and terms of reference in the municipality’s procedure by-law together with the names of the currently appointed chairmen and members.

Some cities and boroughs have a Board of Control composed of the mayor and two or four controllers who are elected at large. It is, in effect, a standing executive committee of the council. But it differs from other standing committees in that controllers are elected at large by the municipal electors. Some of the duties of a Board of Control are laid out in *The Municipal Act*; they include the preparation of a budget, the calling and awarding of tenders, the hiring and firing of appointed department heads and — a real catchall — any other matter which the council gives it to look after. The council as a whole cannot obstruct or alter the actions of a Board of Control, except by a two-thirds majority.

Incidentally, it is the Board as such which has authority, not the individual controllers. In the same way as a member of the council has no authority to speak or act for the council as a whole, so a member of the Board of Control does not speak or act for the Board as a whole.

Appointed officials

The day to day details of municipal administration and advice on policy are the concern of appointed officials. There is great variety in the duties, terms of reference and titles of the officials in different municipalities because they are determined by local practice.

The Municipal Act requires a municipality to have a clerk, a treasurer, one or more tax collectors and an auditor. These officials are appointed by the council and, with the exception of the auditor, hold office at the pleasure of the council. *The Municipal Act* requires the clerk to keep the books, records and accounts of the council (but not of the corporation). The treasurer is required to receive, keep and pay out all the corporation's money; he is also responsible for the preparation and publication of financial statements of the municipality.

The head of the council is an “officer” and, according to *The Municipal Act*, he is the chief executive officer of the municipal corporation. In practice, his executive duties are performed largely by the appointed officials and members

of their staff — except in small municipalities.

For most of their duties, the appointed officials find their terms of reference set by the council in the by-law appointing them, or in the procedure by-law. One appointed official may wear several hats including those of clerk, treasurer and collector. In smaller municipalities, officials serve part time only. In larger municipalities, titles may be given to officials which indicate that their function is broader than that required by statute, such as “Commissioner of Finance”, “Chief Administrator” or “Manager”. Except where provincial legislation or a council by-law indicates otherwise, all appointed officials are accountable directly to the council for carrying out the duties assigned to them.

Although it is seldom included in the by-law, appointed officials often consider it to be their responsibility to recommend policy decisions to the council — even without being requested to do so. They also advise the council on the full effect any of its decisions will have. Municipalities which do not have officials who are qualified in such fields as law, finance, engineering or planning often obtain advice by using the services of professional consultants.

Local boards

To understand what is meant by “local board”, you should refer to the definition in *The Department of Municipal Affairs Act*. Part of this definition reads:

“Any board, commission, committee, body or local authority established or exercising any power or authority under any general or special Act with respect to any of the affairs or purposes, including school purposes, of a municipality.”

This all-inclusive definition sweeps in a great variety of organizations. It includes boards which are obviously part of the municipality, such as a library board and a public utilities commission. It can also include hospitals which are owned by the municipality, community centres, conservation authorities and suburban road commissions.

Legislation requires municipalities to establish local boards for some services, but not for all. So some municipalities provide services such as parking, water, recreation and social and family services through committees of the council; other municipalities have opted to establish a local board for these purposes. A useful dividing line between a local board and a committee is that a *local board* is established under authority of legislation; a *committee of the council* has only the authority given to it by council.

You may have difficulty in deciding whether an organization in your community is a local board of the municipality or a non-government institution. Many health, social and recreational services are provided by private organizations (sometimes

subsidized by a grant from the municipality). Examples include hospitals, homes for the aged, day nurseries for children, animal shelters, skating rinks and golf courses. Children’s Aid Societies are not local boards; emergency measures organizations are. The distinction is important. As the auditor of the municipality, you are automatically the auditor of all the local boards of the municipality.* You must know the organizations for which you have a responsibility.

Local boards also vary in their relationship to the council, to the electorate, and to provincial government departments. The extent to which a local board is accountable to the council is determined by the statute under which it was established; there is diversity from complete accountability to almost complete autonomy.

The council may appoint and dismiss the members of some boards. However, some board members may be directly elected (as in the case of public utility commissions), or appointed by the provincial government (as in the case of police commissions).

Most local boards are dependent on the council for their revenue and for capital funds. However, some boards (such as public utility commission) generate sufficient revenue from their own operations to be self-supporting, except for major capital expenditure. Still others (such as homes for the aged and emergency measures

*School boards are an exception. They appoint their own auditors.

organizations) receive substantial grants direct from the province while obtaining additional revenue through the council.

Local boards may not operate their own bank accounts unless provincial legislation gives them authority to do so. Community centres and recreation commissions, for example, do not have this authority. In these cases the handling of the local board's money is the responsibility of the treasurer of the municipality. Many municipalities appoint the municipal treasurer as the treasurer of all their local boards, which makes a central accounting staff available to all the separate organizations and provides better co-ordination in cash flow.

The most complete autonomy from both the municipal council and the electorate is possessed by organizations which are joint boards of several municipalities, with their members appointed by the councils and their costs shared by the supporting municipalities. Conservation authorities are an example. Generally, they are responsible for an area which, while including parts of several municipalities, is not coterminous with any of them. Health units, social and family services and homes for the aged are frequently managed by joint boards.

Every municipality has different types and numbers of local boards. For this reason, we cannot describe each board in detail here, nor can we detail information about the legislation under each was established. You must first

determine what local boards your client has and then see how they fit into the accountability pattern of the municipality.

The current situation

Each municipality was established to provide service to a particular group of people, living within a geographically defined area. The needs of that group of people were — are — and will be — different from the needs of any other group. Each municipality adapts itself to meet the demands of the changing situation as it attempts to improve the quality of life of its inhabitants. Since the aspirations of one group are different from those of any other group, the priorities of local government differ from municipality to municipality.

The urban expansion taking place in many parts of Ontario is both rapid and loaded with problems. People have come to expect an ever-rising standard of living — and, for municipalities, that means an increase in both the number and standard of services. In most cases, rapid urban growth is beyond the resources and organization of the traditional type of municipality.

New municipal structures have had to be developed. It is for this reason that new regional and metropolitan municipalities are being created, and a radical restructuring is taking place in other areas. It is important to notice that a separate solution is being found for the problem in each area —

a separate research study has been conducted for each particular situation. Local inhabitants have been involved in the planning of the new municipalities so that their particular needs and aspirations might be met in the resulting legislation.

At the same time, certain services have been reorganized to provide better results. Education is now organized to operate under larger and stronger

boards of education. The administration of justice and the assessment of property are now organized on a province-wide basis.

Even more challenging changes are likely in the near future. There will be a restructuring of the system of financing municipalities and changes will be made in the system of grants and subsidies to keep pace with contemporary requirements.

THE MUNICIPAL AUDIT

As in a business audit, both the law and the accounting profession require you to fulfil certain responsibilities. In addition, there are a number of peculiarities attached to the audit of a municipality in Ontario about which you should know.

Your legal duties

The principal legislation which governs your audit is *The Municipal Act* and *The Department of Municipal Affairs Act*. These Acts also authorize the

Department of Municipal Affairs to prescribe the duties of municipal auditors.

In 1970, the Department has directed that the duties of a municipal auditor shall be:

To report to the council, inhabitants and ratepayers whether, in his opinion, the financial statements present fairly the financial position of the corporation and the results of its operations for the period under review in accordance with accounting principles generally accepted for Ontario municipalities applied on a basis consistent with that of the preceding period, if any.

And to make further comment if:

1. the corporation's financial statements are not in agreement with its accounting records
2. the corporation's financial statements are not in accordance with the requirements prescribed by the Department of Municipal Affairs
3. he has not received all the information and explanations that he has required
4. proper accounting records have not been kept, so far as appears from his examination
5. the municipality or any of its local boards has undertaken any capital work, the cost of which has been or is to be paid from the proceeds of a debenture issue, or is to be raised from future revenues in a year beyond the term of the present council, without the prior approval of the Ontario Municipal Board, and which has not been fully disclosed in the notes to the financial statements.

To make such examination as will enable him to report to the council, inhabitants and ratepayers, as required.

Notice that these currently prescribed duties are almost exactly the same as those required of auditors appointed under *The Corporations Act*. The major difference is the requirement for the auditor to comment under condition 5. The reason for this requirement is that a municipality can find itself in serious financial and legal difficulties if it has not obtained prior OMB approval to commit itself to long-term financing beyond the life of its present council. (See page 48).

So much for the duties demanded of you by — or under the authority of — *The Municipal Act* and *The Department of Municipal Affairs Act*. Other provincial government agencies and departments also assign duties to you from time to time. Generally speaking, these extra duties relate to grant claims made to the department or agency concerned. For example, in the case of grant claims for schools and libraries to the Department of Education, or in the case of claims for capital grants for the construction of community centres to the Department of Agriculture, you will be required to sign an auditor's report applicable to the claim.

Professional obligations

When you accept the responsibility for auditing a municipality, you hold yourself out as being capable of executing the assignment with professional proficiency and care. And, if you are a chartered accountant, you are obliged to comply with the professional

standards and recommendations laid down by the Institute of Chartered Accountants of Ontario (Ontario Institute) and the Canadian Institute of Chartered Accountants (CICA).

The client's expectations

Your municipal client engages you as a professional auditor and expects to be charged a professional fee, but by the same token, it is entitled to expect work of professional quality. For this reason it is imperative that you acquire a full working knowledge of municipal operations, municipal accounting and the various statutes and regulations concerned with local government. This body of knowledge is extensive: it will include, for example, complete familiarity with

- the relationship that exists between provincial and municipal governments
- the accounting principles, organization and financial practices of various local government units
- the established duties of appointed officials and elected representatives
- the structure and responsibilities of your client's committees and local boards
- the procedure by-law and administrative policy decisions of the council
- the corporation's policy for such matters as the financing of subdivision development and capital expenditure.



. . . when you accept the responsibility for auditing a municipality, you hold yourself out as being capable of executing the assignment with professional proficiency . . .

You may react to this statement by feeling that it is unreasonable for you to have to obtain this depth and breadth of knowledge — especially if you are undertaking your first municipal audit. After all, the art of local government is somewhat esoteric! Nevertheless, if you intend to audit a municipality you must either become a specialist yourself or make sure you have a municipal specialist on your staff.

Standards of the Ontario Institute

Opinion No. 6 of the Institute applies

to all audits — including those of municipalities, but Standards 3, 6a, and 7, require further comment in connection with a municipal audit.

The third auditing standard of *Opinion No. 6* requires a study and evaluation of internal control. While actual techniques of evaluation vary from auditor to auditor, the basic approach is the same — and it applies equally to all audits, including those of a municipality. The CICA has identified six steps in the study and evaluation of internal control:

Opinion No. 6

- (1) The examination of the records and underlying data is to be performed by a person or persons having adequate technical training and proficiency in auditing, with due care and with an independent state of mind.
- (2) The work is to be adequately planned and properly executed. If assistants are employed, they are to be adequately supervised.
- (3) There is to be an organized study and evaluation of internal control as a basis for reliance thereon and for the determination of the extent of test audit procedures.
- (4) Sufficient appropriate evidential matter is to be obtained through inspection, observation, enquiry and confirmation to afford a reasonable basis for expressing an opinion on the financial statements.
- (5) The disclosures in the financial statements are to be regarded as reasonably adequate unless the report states otherwise.
- (6) The report of the auditor
 - (a) shall state whether the statements are presented in accordance with generally accepted principles of accounting, and
 - (b) shall state whether such principles have been consistently observed in the period under review in relation to the preceding period.
- (7) The report shall contain an expression of opinion on the financial statements taken as a whole or an assertion that an opinion cannot be expressed. In the event that an opinion cannot be expressed, reasons should be given.

Reasons for expressing no opinion on financial statements as a whole may involve: lack of sufficient evidential matter, serious limitations in scope of examination, or unusual and very material uncertainties concerning asset valuations or liability determinations. When an auditor expresses a qualified opinion, the nature of the qualification should be clear and, in addition to the reasons for the qualification, the effect of the item in question on the financial position and the results of the operations should be shown if these matters can be determined.
- (8) Where no audit has been performed or the auditing procedures are insignificant in the circumstances, any financial statements with which the member is associated, whether prepared on his stationery or not, should be clearly marked as unaudited whether other comments are made or not. If the member believes that unaudited financial statements are false or misleading, he should refuse to be associated with them in any way; continued association with such statements even though they are marked as "unaudited", is not satisfactory professional conduct.

1. Identify the accounting system and controls.
2. Make a preliminary evaluation of the system.
3. Determine the extent of and carry out tests of the system.
4. Assess the results of procedural tests.
5. Consider alternatives if controls are inadequate or ineffective.
6. Make a final evaluation of the system of internal control.*

The sixth auditing standard of *Opinion No. 6* calls for you to report whether your client's statements have been presented in accordance with generally accepted accounting principles. Your *Municipal Finance Manual* contains instructions and procedures which, if followed, result in the application of municipal accounting principles acceptable to meet the requirements of standard six.

The seventh auditing standard of *Opinion No. 6* requires you to state why you cannot express an unqualified opinion on your client's statements. This matter is one of communication and you should be unequivocal in giving reasons.

Recommendations of the CICA

On accounting principles

The *CICA Handbook* contains

accounting principles which apply to municipalities except where they are modified either by instructions and procedures in your *Municipal Finance Manual*, or by the specific nature of a municipality. For example, *Net long-term liabilities* and *Capital outlay to be recovered in future years* require different reporting treatment in the financial statements of a municipality. As a rule: where your *Municipal Finance Manual* is silent on financial statement presentation, be guided by the *CICA Handbook*.

On auditing

You will find that most of the *audit* recommendations of the Accounting and Auditing Research Committee in the *CICA Handbook* are applicable to municipalities and you should regard them as a guide to your conduct.

The *CICA Handbook* recommends that your report should contain a direct reference to the scope of your examination. As well, you should indicate clearly the financial statements which are covered by your examination and opinion. (A model form of auditor's report is shown on page 28. This model is an adaptation of the form suggested in the *CICA Handbook*). To repeat: if you find you cannot express an unqualified opinion of the fairness of your client's financial statements, say so without equivocation, and give your reasons for qualification clearly and precisely — as suggested by the *Handbook*, and as required by *Opinion No. 6*.

*CICA Study Group on Audit Techniques, *Internal Control and Procedural Audit Tests*, 1968, p. 2.

Features of the municipal audit

Accounting principles and financial statement presentation

Where accounting principles “generally accepted for Ontario municipalities” (see suggested auditor’s report) differ from other generally accepted accounting principles, the differences are contained in the *Municipal Finance Manual*.

The form of financial statement presentation to be used by all municipalities in Ontario is established by the Department of Municipal Affairs. The Department works closely with committees of the Ontario Institute and the Association of Municipal Clerks and Treasurers of Ontario as well as consulting individual municipal treasurers and auditors. In this way, there is an ongoing revision aimed at constantly improving the reporting standards of municipalities and the usefulness of the prescribed financial statements.

The Auditor’s Report

The Department does not lay down the form your report should take. However, the Municipal Accounting and Auditing Committee of the Ontario Institute has agreed that the form on page 28 meets all professional requirements when an unqualified opinion is to be expressed.

During the course of your audit of a municipality, you will be required

to report on the financial statements of several local boards as well as on those of the municipality itself. (See page 29).

The salutation in the suggested form is suitable for your report on the complete package of financial statements of the municipality and its local boards in your client’s annual Financial Report. The same salutation can also be used for your report on the basic statements of the municipality itself — such as those used for newspaper publication or for sending to each ratepayer (see page 31). But each local board has a different position in the overall accountability pattern of the municipality; and when you report on the financial statements of a local board, you will need to select the appropriate salutation.

The reference in the suggested form of Auditor’s Report is suitable for your report on the complete package of financial statements in the annual Financial Report — it refers to the Index at the front of the Financial Report. Other forms of reference are feasible, so long as they make clear what documents are covered. For example, when you report on the statements which are published or distributed to ratepayers, you could list the name of each financial statement.

The supporting schedules contain extensive information. You need not concern yourself with insignificant details in these schedules, but you must bear in mind that users of the information they contain — your client,

AUDITOR 'S REPORT

To: The Members of Council, Inhabitants and
Ratepayers of the Corporation of the
.....of.....

We have examined the 19...financial statements
of the Corporation of the.....
of..... and its local
boards, which are listed on the attached Index.
Our examination included a general review of
the accounting procedures and such tests of
accounting records and other supporting evidence
as we considered necessary in the cirsumstances.

In our opinion these financial statements present
fairly the financial position of the Corporation
of the.....of.....
and its local boards as at December 31st, 19...,
and the results of their operations for the year
then ended, in accordance with accounting prin-
ciples generally accepted for Ontario municipal-
ities applied on a basis consistent with that of
the preceding year.

(Signed) _____

City
Date
Licence Number

the provincial government, bond dealers and other people interested in local government finance — expect it to be reliable. You only cast doubt on the integrity of this information if you specifically deny an opinion on the fairness of the supporting schedules.

You should ascertain the reasonableness of these schedules during the course of your study and evaluation of internal control.

The auditor

Appointment, dismissal, powers and rights

Your appointment is made when the council of a municipality passes a by-law to that effect. *The Municipal Act* guarantees your office “during good behavior”. And when you are appointed the auditor of a municipality, you automatically become the auditor of all that municipality’s local boards. At the same time, you become the auditor of any joint board (see page 20) supported by your client for which it is liable for a larger portion of the

operating costs than any other municipality (except boards of education and separate school boards).

You cannot be dismissed except for cause. Your appointment is of a quasi-permanent nature; the council — should it decide it has a proper reason to dismiss you — must pass a by-law with a two-thirds majority. You must be notified of the meeting at which your dismissal is to be discussed, and you are entitled to attend this meeting and be heard on the subject. “Cause” is not defined by the law, and for that reason, is subject to various interpretations. If, after private discussion with you, your client decides to change its auditor for any reason you consider sufficient, you will probably want to accept the situation and co-operate with your successor. *Opinion No. 16* of the Ontario Institute, while referring throughout to the position of an auditor appointed under *The Corporations Act*, is applicable in principle to a municipal auditor. In particular, your responsibility is to protect the rights of the inhabitants of a municipality, just as in a business corporation appointment your responsibility is to the shareholders.

Opinion No. 16

Resignation of Auditors: On occasion, the question arises of the duty of a chartered accountant appointed to act as an auditor at the annual general meeting of an Ontario or Canadian company, who is asked by the *directors* to resign before reporting. . . .

In summary the auditor of a company is appointed to represent the shareholders and has a duty to them, he should never lightly resign his

appointment before reporting and should not resign at all before reporting if he has reason to suspect that his resignation is required by reason of any sharp practice, impropriety, or concealment, which it is his duty to report upon. Subject to that general statement, however, there may be exceptional circumstances in a particular case which would justify his resignation and this will be a matter of individual judgment in each case.

You have extensive powers as a municipal auditor. *The Municipal Act* guarantees you the right

- to demand to see any documents of the municipality at any reasonable hour
- to require any member of council or appointed official of the municipality to provide you with any information or explanation you need
- to be notified of, and to attend, any meeting of the council, and to be heard on any part of the business of the meeting that concerns you as auditor
- to require any person to give evidence on oath.

Traditional role

Traditionally it has been a responsibility of auditors at all levels of government to ensure the absence of technical irregularities by seeing that

- money was not spent for illegal purposes
- regulations for uniform accounting and financial procedures were observed
- accounts were kept correctly and honestly
- the budget was observed and spending kept within its limits.

In the past municipal auditors have been expected to perform at least a

part of this traditional role. Today, however, in a well administered municipality, the likelihood of technical irregularities is minimized by an adequate system of internal control. If your evaluation of this system is reliable, it should not be necessary for you to examine every transaction of the municipality for its legality. Appointed officials, acting within their terms of reference established by the council, are responsible for administering your client's affairs in accordance with the relevant legal requirements.

Meeting the requirements of the Department

Licences

While your appointment is a matter between you and your client, you must have a municipal auditor's licence from the Department of Municipal Affairs. Your licence number must be stated on your report. (See page 28).

Filing annual reports

It is your client's responsibility to file a copy of its annual Financial Report, including the financial statements of all the local boards, with the Department of Municipal Affairs by March 31 of the following year. You may wish to provide this service on behalf of your client.

Filing auditor's reports

When you make a report to the council on any matter which relates to your audit, send a signed copy to the Depart-

ment of Municipal Affairs. This requirement includes original, amended or supplementary auditor's reports — and any reports concerning defalcation or irregularity. Apart from this requirement, you may feel there are problems developing in a municipality of which the Department should be kept informed. If so, it will be glad to receive a report from you.

Publication or distribution of financial statements

The Municipal Act requires that a copy of your client's financial statements, together with your report, be published or distributed. Any notes which apply to these statements should also be published.

Dealing with defalcation, control weaknesses, and material illegalities

The general public — including the inhabitants of your client municipality — is greatly concerned about the misappropriation of public funds. Whatever may be your true obligations, most laymen persist on looking upon the municipal auditor as their main safeguard against fraud; if it exists they expect you to uncover it! Of course, your prime function is not that of discovering embezzlement — and there is certainly no greater legal or professional obligation on you to do so in a municipality than there is in a business audit.

When you discover control weaknesses during your audit, your reaction will

depend upon your judgment of their importance. You should not hesitate to report all control weaknesses, together with your recommendations for improvements, to the appropriate level of responsibility in the municipality. You will probably decide to deal with the treasurer or with other appointed officials in routine matters. However, more important problems should be dealt with in a report addressed to the council, or to the head of the council.

Even in the best administered municipalities, mistakes and illegalities can occur. If your client has engaged in activities or entered into contracts which are beyond its legal powers, it exposes itself to contingent liabilities. You must decide whether or not these liabilities are material. You can ask your client to seek the advice of its solicitor in determining its authority for its actions — and you should feel free to seek separate legal advice if there is any uncertainty in your mind. But in the final analysis, the decision on materiality is your own. Remember that it generally serves no useful purpose to attract attention to potential liabilities which are not material. You may find *Materiality in Auditing* (a CICA publication) a useful guide. If a material contingent liability exists, it is reflected in the *Notes to Financial Statements*; if it is not, you should disclose it in a qualification of your report.

While many of the problems mentioned above are of a routine nature, there will be occasions where fraud, control

weaknesses, illegalities or abuse of office affect your opinion on the fairness of a municipality's financial statements. In such instances, you must report the facts to the inhabitants and ratepayers of the municipality. Officers of the Department of Municipal Affairs are available to discuss the matter with you and they may be able to help you decide how to proceed.

Providing special services

If you restrict your services to what is legally and professionally necessary, you can do a satisfactory job and justify a reasonable fee. But if you accept the challenge available to a municipal auditor, you will have many opportunities to provide your client with service beyond your normal audit function.

One of the most frequent opportunities you may have for rendering special services is in helping your client expand its accounting or information system to cope with demands of growth and change. Few municipalities have adequate staff resources to keep up-to-date with every advance and advantage of modern business methods. You are probably the professional advisor who is best able to help your client improve its accounting and information systems. Indeed, you may be selected as municipal auditor on the basis of your knowledge of finance and accounting and on your consequent ability to contribute to the improvement of your client's operation.

Another service you can offer is your

assistance in preparing both the current and long-term budgets. The setting of expenditure priorities and financing policies is a responsibility of the council — but the task of putting together a package of budget information is a task which may challenge the most proficient municipal treasurer. You might well make an informed review of the budget to help ensure that the information in it will enable members of the council to grasp clearly the effect of new projects, rising costs or changes in the provincial government grants.

As we mentioned on page 20 many municipalities are considering the benefits and costs of amalgamating into larger units. Before an amalgamation takes place, a vast amount of financial information is required for effective planning. Here you can render an invaluable service in helping your client effect a worthwhile study of its future organization.

Your client may wish you to help it upgrade its personnel in the treasurer's department. As knowledge grows increasingly specialized, it is becoming impossible for a personnel officer to interview, hire and train new staff without the advice of an expert. Your opinions will be valued highly in setting policies for staff selection and training.

But perhaps the service you are best equipped to offer is that of introducing improved business methods. In fact, unless someone with your combined knowledge of your client's problems and

your general business experience strives to find ways of increasing municipal administrative efficiency, the existing system may never improve. No doubt — as a part of your regular audit — you will advise your client of any weaknesses you have observed in its system of internal control. When you go further and offer your advice on methods of improvement, you provide an invaluable service because you will stimulate an increased awareness of possible improvements in operational efficiency.

You should have a clear understanding with your client on the services you provide in addition to your regular audit. The by-law which appointed you should be supplemented by letters of agreement covering the extent and fee for any special services which

are additional to your audit. You can also avoid misunderstandings if you distinguish between your audit and your special services by billing each separately.

One final word. Elected representatives and appointed officials are, with rare exceptions, dedicated servants of public, striving to improve the quality of the environment within their municipality as effectively as possible. Local government is complex, urban communities are expanding rapidly, and their inhabitants are demanding an increasing level of service. You have the opportunity of sharing in meeting the needs of the future: not only in challenging professional work but also in contributing to the improvement of the quality of government in your client municipality.

Municipal revenue is reported under three headings:

- taxation
- contributions from other governments, and
- other revenue

These headings and their respective accounting treatments are explained in your *Municipal Finance Manual*, which forms a useful background to this chapter. As explained on page 25 of this book it is expected that you will use some form of system review as a basis for your audit.

Basic elements of internal control

The systems for controlling municipal revenues and cash receipts differ from one municipality to another. They range from cash to accrual accounting and from hand-written receipts to complex computer operations; the level of sophistication depends upon local circumstances. However, the systems are, in essence, the same as you find in a business corporation. You can evaluate your client's internal control only after you have made a detailed investigation of its systems.

Before you begin your audit, look through the by-laws and identify the policies fundamental to the revenue systems. Included in these policies are the delegation of responsibilities for billing and collecting revenues, agreements with other municipalities, and fees charged for municipal services.

Tax billing and collection policies — including the use of interim tax bills, dates of tax instalments, rates of penalties and interest on tax arrears, and authority to use tax sale or registra-

tion procedures must be approved by a council by-law.

The council sets (or delegates its authority to set) licence and parking meter fees, charges for the use of municipal facilities (such as arenas and golf courses) and rates to be charged for municipal services. If the council has entered into a joint agreement with another municipality the details are in the by-law ratifying the agreement.

The treasurer — the appointed official most closely involved in the control of municipal revenues — has a statutory duty “to receive and safely keep all the money of the corporation”. Usually the council assigns him other, far more extensive, duties. They include:

- developing an accounting system to control municipal revenues
- compiling the municipal estimates
- preparing the revenue budget
- advising the council on optional methods of raising revenues
- maximizing miscellaneous revenues such as short-term interest

- centralizing the accounting for the revenues of local boards to increase control

When you review internal control over municipal revenues you should remember that almost all major defalcations in municipalities have involved misappropriations of income.

Features of municipal revenue

Taxation revenue

Upper tier municipalities

Counties and other upper tier municipalities do not tax directly but apportion their revenue requirements over their supporting municipalities. The method used by counties to apportion costs is explained in the Instruction for the supporting schedule entitled “Basis of Apportionment of County Levy” in the *Municipal Finance Manual*. Members of the Department of Municipal Affairs are glad to tell you about the methods used by regional governments for apportioning costs.

Lower tier municipalities

Taxation is the major source of revenue under the direct control of the municipal council, and it is primarily the municipality’s ability to raise future taxes that determines its financial strength. The system used for raising taxes is unlike any method of revenue raising used by business corporations. The background to municipal taxation is

discussed in *The Report of the Ontario Committee on Taxation*, (*The Smith Report*), Vol. II, pages 53-61, which explains why the system has evolved to its present rather complex form.

The assessment roll

The roll which determines the basis of the allocation of taxes is prepared by the Assessment Division of the Department of Municipal Affairs. The assessment commissioner who prepares the assessment roll delivers it, together with his affidavit attesting to its accuracy, to the municipality by October 1 of the year preceding taxation, unless the Minister approves its late delivery. Changes in the roll are not permitted — except as provided by statute. Once the roll has been delivered, all changes entered in it are the responsibility of the municipal clerk — although changes are made by the assessment commissioner in his records. An assessment may be appealed by any person — including municipalities and school boards. The appeal system is described in detail in Appendix B, page 63. It permits appeals to the Assessment Review Court and thereafter further appeals to courts of law.

The basis for calculating mill rates is the assessment roll corrected and revised by the Assessment Review Court and certified by the regional registrar of the court — plus the addition of other assessments made before December 31 in the year prior to the taxation year. The municipality reviews the assessment roll for errors before

using it. Examples of tests that are often conducted are:

- comparison of building permits and water connections to the supplementary assessment rolls in order to ensure new properties are assessed upon completion.
- review of the previous year's supplementary assessment rolls to ensure that all the properties entered therein have been correctly entered on the new assessment roll.
- check of properties for incorrect classification — especially tax exempt properties — to prevent unnecessary loss of revenue to the municipality
- comparisons of assessment totals to previous years to test for any obvious errors
- comparison of the ratio of assessment to population with that of previous years to verify reasonableness of the roll
- review of assessments for possible appeals to the Assessment Review Court
- comparison of properties on a map to the assessment roll to check omissions. (This type of test can be very difficult to conduct in a rural municipality, however)

Errors in assessed population can result in a reduction in the unconditional per capita grant — as well as a loss

of taxes from missed assessment; they can also result in a misallocation of the municipal taxation burden. The only way a municipality can ensure equity is to review the assessment roll thoroughly.

Mill rates

A municipality calculates mill rates by using this formula:

$$\frac{\text{Total taxation revenue required} \times 1000}{\text{Total taxable assessment}}$$

The resulting mill rate is then used as a factor which is applied to the assessed value of each taxable property in order to calculate the amount of tax payable. Mill rates for residential and farm, commercial, business and special area rates must be approved by the council in a tax rate by-law.

Residential and farm assessments are taxed at a lower mill rate than commercial property; residential and farm owners pay 10% lower school taxes than do commercial property owners. Moreover, only residential and farm owners benefit from the unconditional per capita grant and from regional grants.

Business tax is calculated by applying the commercial mill rate to the assessed value of the real property used for business purposes, as laid down in *The Assessment Act*. Rules for calculating the special taxes on telephone and telegraph, transportation and pipeline companies are also laid out in that Act. Business taxes are

a charge against the owner of the business and not against the owner of the building in which the business operates. Therefore, in collecting unpaid business taxes, a municipality has the right to seize the chattels of the business in default — but not the real property.

Often, the ratepayers in a portion of a municipality request a special service which is not provided to all ratepayers. The council can then tax those ratepayers to pay for the special service. (Rules covering the expenditure of these special area mill rates are on page 45).

Transitional provisions, such as those contained in the legislation creating regional governments and county school boards, have resulted in a series of unusual rules which must be observed in calculating mill rates.

The collector's roll

The collector's roll takes many different physical forms such as ledgers, copies of tax bills, and accounting machine print-outs; it is compiled by extending the individual assessments in the final assessment roll by the mill rates and then adding the special charges. The collector's roll records against each property and business, all taxes — plus other amounts added to the tax bills — for the year. Uncollected charges from prior years are not included. It is imperative that municipal officials ensure that all

changes made to the assessment roll are reflected in the collector's roll.

Preparation of tax bills

The council establishes policies setting dates when taxes are due. There is no statutory limit to the possible number of tax instalments, and taxes of up to 50% of the previous year's mill rates may be raised on an interim levy before the current annual revenue estimate is set. The council may also decide on a minimum tax bill of six dollars for each property.

Sometimes special charges, which are not calculated from mill rates, are billed to some taxpayers. Some of these special charges (such as local improvement and drainage charges) create accounting problems because a project results in a different charge for each property affected; your client's accounting system must be adequate enough to allocate each charge correctly. These special charges represent a form of taxation that must be shown separately on the financial statements. Other charges (such as hydro arrears, which do not represent taxation) can be added to the tax bill for collection.

Supplementary taxes

Whenever new assessment is added during the taxation year — either from the correction of an omission from the roll or from new construction — supplementary taxes arise. The rules for raising taxes on these additional properties are defined in *The Assessment Act*. The law requires that supplementary taxes from new construction

be distributed on a pro rata basis to school boards, counties and regional governments. Some municipalities also distribute supplementary taxes raised as a result of an error in the roll. The amount of supplementary taxation from new construction is affected by the date when the provincial assessor adds it to the assessment roll; additions to the roll are taxed according to the portion of the year they are on the roll. Therefore a delay in assessing results in a loss of revenue to the municipality.

Collection of taxes

A municipality charges penalties and interest on overdue taxes in order to encourage prompt payment. Penalties are charged for tardy payment of taxes in the year they become due, while interest is charged on arrears remaining after that year. The council passes a by-law stating the rates to be charged within upper and lower limits set out in *The Municipal Act*.

An adequate system of control is developed by the municipality to ensure that applicable penalties and interest are always charged and paid. In this way, a loss of revenue to the municipality is prevented.

A municipal corporation may act through the division court and use bailiffs to obtain payment of taxes — as soon as they become due. It also has final recourse to two special procedures to enable it to collect overdue property taxes: tax sale and

tax registration.* *The Municipal World* issues booklets listing the section of the statutes and regulations involved in each procedure (see bibliography). In the first instance, every municipality is required by *The Municipal Act* to use the tax sale procedure. However, the council can pass a by-law to transfer to the tax registration procedure. In some cases a county petitions the DMA to have all its constituent municipalities transferred onto tax registration, in which case every municipality involved must use the tax registration procedure.

Contributions from other governments

The statutory requirements and the unique nature of these contributions make necessary special internal control considerations.

The instructions in your Municipal Finance Manual for the supporting schedule entitled “Analysis of Revenue” outline the major sources of contributions from other governments under three headings:

- payments in lieu of taxes,
- subsidies, and
- payments from other municipalities.

Payments in lieu of taxes**

The accounting controls over payments in lieu of taxes are usually straightforward.

**The Smith Report*, Vol. II, pages 285-286
***ibid.* pp. 136-151.

Properties subject to payments in lieu of taxes are shown as tax exempt on the assessment roll. After the mill rates are set the municipality is required to bill the appropriate body in order to obtain payment.

Some bodies do not pay the equivalent of full mill rates: for example, Ontario government property does not normally pay the equivalent of school rates. When less than full mill rates are used to calculate the payment in lieu of taxes, details and explanations are available in the municipal records and in the appropriate legislation.

Payments from some government bodies take a long time, so the accounting system must be capable of providing control over this revenue.

Subsidies

Subsidies from the provincial government are a complex and rapidly changing form of municipal revenue that is difficult to audit.

Background details on most of the important programs, such as road and health and welfare subsidies, are readily available.[†] Note that the *Municipal Finance Manual* tells you to include mining revenue payments under subsidies from the province of Ontario.[‡]

There are two main sources of information about provincial subsidy programs: a regularly updated manual, *Provincial Assistance to Municipalities*,

Boards and Commissions, (see bibliography) and the information offices of provincial government departments and agencies.

Payments from other municipalities

The Municipal Act authorizes a municipality to enter into an agreement with another municipality for a joint project for any purpose within the jurisdiction of the councils concerned; the resulting joint venture may result in payments being made between municipalities. Details of such agreements are included in the appropriate municipal by-law. You should also review the rules about netting income with expenditure outlined in your *Municipal Finance Manual*, page 202, before you decide on the proper accounting treatment.

Other revenue

The *Municipal Finance Manual* outlines the chief sources of other revenue.

The revenue audit

Adaptations of normal audit procedures are only suggested in this section — always use the procedure you feel is most appropriate to the circumstances.

General

When you begin to review your client's revenue system you should obtain

[†] *ibid.* pp. 409-437. See also J. S. Dupre, *Intergovernmental Finance in Ontario* (Toronto: Queen's Printer).

[‡] *ibid.* pp. 171-191.

a copy of its budget; it provides details of all major sources of revenue; it also lets you know how much revenue is expected. At the year end, variation between the budgeted and actual figures may indicate that further investigation is required.

An error in the revenue system may result in a material misallocation of the tax burden among ratepayers. For example, where the unconditional per capita grant is not used for the exclusive relief of residential and farm ratepayers, they may be materially over-taxed. So, in addition to the usual problems of measuring materiality in the effect on the financial statements, you should also consider the effect of error on an individual ratepayer.

Taxation revenue

You should review the taxation revenue of the municipality by considering the taxable assessment, the annual estimates and the effect of statutory provisions (such as unconditional per capita grants and the transitional provisions in the legislation creating regional governments and county school boards).

The law requires your client to levy all supplementary taxes provided for by statute, including

- taxes on new construction which has been assessed since the return of the assessment roll on which the year's original tax levy was calculated

- taxes which should have been included in the original tax levy, or in prior years' taxation, but were excluded because of errors or omissions in the roll

Your client may not exercise discretion about supplementary taxation. Failure to bill and collect these taxes results in revenue for the year being understated in the financial statements.

Your interest in the accuracy of the assessment roll is crucial because it has a bearing on whether the taxation revenue for the year is fairly reflected in the financial statements. But you need not concern yourself with the valuations in the assessment roll; they are the responsibility of the assessment commissioner and are subject to appeal procedures (appendix B).

Nevertheless you should be concerned about whether or not your client has made an adequate review of the assessment roll to ensure that

- any properties omitted from the assessment roll are billed the correct amount of supplementary taxes
- any new construction (which was not included in the assessment roll from which the original tax levy was calculated) is billed for the correct amount of supplementary taxes.

When you audit an upper tier municipality you have no direct involvement with assessments and collectors' rolls. However, you have a responsibility to assure yourself that the method

of apportioning the annual estimates over the supporting municipalities is in accordance with the law. An error in apportionment might result in a material misallocation of the tax burden.

You may find the procedures outlined in the CICA audit study *Confirmation of Accounts Receivable* are a useful guide when you plan your tests of taxes receivable. Both the CICA audit study and Handbook suggest that when internal control is not effective, confirmation should be made at or near the year end.

Contributions from other governments

You can confirm the amounts paid to the municipality during the year by contacting the appropriate government department or agency, or the other municipality, which made the payment. A list of the addresses of the offices in provincial departments and agencies that pay subsidies is in the *Municipal Finance Manual*. Government departments and agencies operate on a cash basis and cannot confirm the balance outstanding at the year end. Alternative procedures such as those outlined in the CICA audit study *Confirmation of Accounts Receivable* should be used together with any other tests you consider necessary in the circumstances.

You should examine the subsidy claim and the paying agency's reaction

to it — was the claim allowed, denied, or only partially allowed? Comparing these forms with month-end or year-end statements will indicate the reliability of the municipality's year end accrual.

Details of payments in lieu of taxes and joint municipal agreements are available in the treasurer's or clerk's office.

Other revenue

The schedule of fees for municipal services, licences, and so on can be traced from by-laws approved by the council. You may find it helpful to prepare a list of these by-laws and update it by looking through the minutes of the council to compare the sources of revenues from year to year. You can also see if there are any new sources of revenue which the municipality has developed.

Wherever necessary, you should press for improvements in control over other revenue. Your influence may result in improvements to the accounting system that will make it unnecessary for you to qualify your report year after year. You are engaged to make a report on whatever you deem necessary. You should not accept the excuse of poor control to avoid this responsibility, but you should continue to impress upon the council the need for improvements until it acts.

EXPENDITURE

The detailed audit is no longer required by the Department of Municipal Affairs. As explained on page 26, your audit depends upon tests of procedures to determine the reliability of the system of internal control — in other words, how you evaluate your client's system of internal control depends on the audit practice you normally follow.

The nature of the municipal structure increases the complexity of your audit of municipal expenditures. As we have explained, each municipality has developed a structure to meet its own local needs; your client has developed the systems and sub-systems necessary to meet the expenditure requirements of its own particular structure. Usually, the power to purchase and receive has been left to each department. The requisitioning and receiving functions will remain decentralized even in municipalities which have central purchasing departments. In your review of internal control, you will have to become familiar with most of the systems in your client's departments.

The systems you are evaluating during the expenditure audit will also be used — with only slight modifications — to process payments for capital expenditures. Your capital audit is therefore partially dependent upon your evaluation of the expenditure system.

The reporting requirements of the Department of Municipal Affairs are set out in *Bulletin 2* of your Municipal Finance Manual. You will find this Bulletin useful background reading to this chapter.

Basic elements of internal control

Introduction

Policy and procedures are dictated by local circumstances, therefore, there are differences between systems of internal control. However, similarities exist between municipalities in their organizational patterns and financial reporting requirements.

Policies and procedures

Policy decisions involving the expenditure system are made by the council

in its procedure by-law. (See page 14). Matters of policy which you should find in a procedure by-law include: the assignment of responsibilities for the control of expenditures, personnel policies, and policies for purchasing and tendering.

Appointed officials establish procedures for purchasing, payment of accounts, preparation of annual estimates, pay-roll compilation, control of inventories, and the preparation and distribution of financial reports.

The standard method used for controlling municipal expenditures is for

the council to allocate responsibilities to various levels of management and then to exercise control by requiring adherence to the expenditure budget.

Allocation of responsibility

The council

The council concentrates its energy on overall control; it defines the type of large or unusual expenditure that requires its explicit approval.

The remaining transactions are handled by appointed officials; with the council using information from the budgets and the financial reporting system to manage the municipality's affairs. The council takes little direct part in purchasing procedures, although there may be exceptions in small municipalities.

Committees

Committees exercise a strong influence in the control of expenditure. If control has been delegated to committees their responsibilities are defined clearly by the council (see page 17).

Department heads

The appointed head of each department usually provides direct control over expenditure. Except where purchasing is centralized, each department is responsible for its own requisitioning, purchasing, warehousing, and approval for payment. The council maintains control over departments by requiring justification of each program before allotting

budgeted funds and department heads control expenditures within budgeted limits. Monthly financial statements provide the information for the department heads to maintain control and for the council to assure itself that expenditures are within the budgeted limits. A department head must always be able to explain any material variances from budgeted expenditure.

The treasurer

Provincial legislation makes the municipal treasurer responsible for the receipt and disbursement of the corporation's money. This concept is a legalistic and limited description of the treasurer's responsibility — the progressive treasurer also provides many other services to improve the municipality's management of expenditures. He

- installs and operates a centralized system for the payment of accounts
- designs, prepares and distributes the internal financial statements
- advises the appointed department heads when expenditures threaten to exceed budget and points out where economies may be effected.

Budgetary and reporting controls

A municipality must have an accounting system that highlights unfavourable expenditure patterns. Well defined budgets and accurate current financial statements should be in such a form that department heads and the council

can readily compare actual and budgeted expenditures.

Every municipality is required by law to prepare and adopt estimates of the amounts required during the year, but your client's budgetary system should far exceed this statutory requirement. The preparation of the good budget follows these general guidelines:

- it is based on objective data and informed opinion
- it is prepared in advance of actual expenditure
- expenses are classified by department so that each appointed department head is aware of his responsibilities and expenditure limits
- each department head becomes involved in the budgeting process and agrees to those expenditure limits for which he is responsible
- expenditures which occur seasonally (e.g. road maintenance, recreation and snow clearing) are budgeted on a seasonally adjusted pattern.

The bibliography at the end of this book gives sources of further background on municipal budgetary control.

Reporting and budgeting controls cannot be separated. A budget is only as effective as the reporting system that compares it to actual expenditures. You should concentrate as much effort on examining the effectiveness

of the reporting system as you do on the budgeting system. Features that you should expect to find in the reporting system include:

- reports prepared on a periodic basis, at least once monthly, made to the council and the appropriate appointed officials
- current financial information in a form suitable for control of expenditure
- variations from budgeted expenditure noted and appropriate action taken

You may have difficulty in deciding where effective financial control is exercised in the municipal structure. In many cases it can be pinpointed only by locating which official takes the necessary controlling action.

Transactions subject to specific statutory control

For many transactions, the law is explicit in restricting the ways in which money may be spent. As the municipal auditor you should assure yourself that these legislative requirements have been met. The more important transactions governed by legislation are:

Earmarked revenues:

Amounts raised by special rates and charges can be paid out only for specified purposes. Some major examples are:

- **board of education rates:** payments of taxes levied on behalf of a board of education are paid to the board in quarterly instalments starting on March 31 — although in some areas local agreements may call for more frequent payments. Provision for early payment discounts and late payment penalties are included in the legislation. Supplementary taxes are paid to the board by December 31 of the year in which they were raised
- **county and regional rates:** payments are made to the county by December 20 of the year during which the revenues were raised and supplementary taxes are paid to the county by December 31. In most cases, local by-laws require payment earlier in the year. Dates of payment to a regional government are established by the regional council. Both county and regional authorities are entitled to charge interest on overdue payments
- **area rates:** these revenues may be used to provide such services as garbage collection, fire protection and street lighting in certain areas of the municipality. They must be used in the area and for the purpose for which they were raised. A surplus at the year-end must be used to reduce the area rate levy in the following year.

Non-cash transactions:

These transactions are those which do not involve the actual transfer

of cash but appear as expenditures in the annual estimates. The most important are:

- **transfers to reserves:** *Bulletin 4* of the *Municipal Finance Manual* makes you familiar with the nature of this type of account. It also explains the limitations on establishing and using these reserves
- **taxes written-off:** taxes may be written-off only in accordance with the provisions of *The Assessment Act*
- **deficits:** *The Municipal Act* requires the council to levy for a deficit in the year following the one in which it was incurred; therefore a deficit is provided for in the annual estimates.

Contributions, grants and subsidies

A municipality makes grants to bodies and in amounts only as permitted by statute. If you have any doubts about the legality of any payment you should ask the pertinent municipal officials to give you their authority for making the payment.

The expenditure audit

While your audit approach should be the same as that for a business client, there are a few wrinkles to auditing municipal expenditures that you need to note.

If you find there is no clear definition of responsibilities between different

appointed officials — or if there are any other material weaknesses in financial control — you should make a report to the council and recommend improvements in the system. Your reaction to any situation should be guided by your professional opinion in the circumstances — materiality should always be considered.

Several provincial government departments employ officials who visit municipalities to examine documents in support of subsidy claims. Their interest is primarily to ascertain whether all legal or engineering requirements have been met and whether all claimed expenses are eligible for subsidy.

Their work does not form an integral part of the system of control within a municipality. Furthermore, the procedure followed, and responsibility possessed, by one subsidy verification officer may vary considerably from that of another.

Test auditing is a valuable technique. However, you may experience difficulty in choosing a representative sample

because municipalities have a tendency to operate on a decentralized basis. (A useful text on how to choose audit samples is *Sampling Manual for Auditors* — see bibliography).

The expenditure patterns of most municipalities are predictable due to their non-volatile nature and the limitations of their budgets. This fact should make variance analysis one of your more important audit tools: an examination of variations between budget and actual expenditure should reveal any unusual patterns for the year.

In addition to the usual difficulty in determining when expenditures are cut off at year end, you may find that your client uses commitment accounting. As a general rule, only the legal obligations of the municipality should be recorded. If goods or services have been ordered but have not been received — and title has not passed — then there is no legal obligation to pay and no expenditure should be recorded. This is the generally accepted accounting principle for year end cut off.

Capital in the municipal context

The word “Capital” has a specific meaning in the municipal context: it is used to describe the transactions of the capital fund, including both long-term (i.e. capital) expenditure and long-term financing. (See page 13). All long-term expenditure — regardless of how it is financed — and all the money that a municipality obtains through long-term financing is reported in its capital fund. Examples of capital financing include: borrowing through debenture issues, contributions from other governments, subdividers’ fees, contributions from the revenue fund for capital expenditure, and private gifts. *Bulletin 5* of the *Municipal Finance Manual* describes the accounting and reporting of capital transactions, while *Bulletin 3* describes the reporting of long-term liabilities.

Major capital projects, by their nature, require a long time to plan, finance and complete. They frequently extend beyond the lifetime of a single elected council and their cost can affect profoundly the financial position of a municipality. For this reason, many restrictions and preliminary administrative procedures have been written into the legislation. When you evaluate the propriety of capital transactions, you must have a detailed knowledge of the pertinent legal restrictions and required administrative procedures.

The provincial government and the Central Mortgage and Housing Corpora-

tion (CMHC) provide substantial capital assistance to municipalities in order to encourage a high standard of service to their inhabitants. You should be familiar with these assistance programs, both in order to perform an effective audit, and also to ensure your client is obtaining the maximum financial assistance available to it.

In most municipalities, each capital project is regarded as unique, and is processed as a separate cost centre. You should organize your approach to the audit of capital accordingly.

The capital project — preliminary steps

Whatever the source of financing for a capital project, there are legal requirements which must be observed in obtaining the financing, as well as desirable administrative procedures.

Long-term financing — minimum procedures

The council passes a by-law to approve long-term borrowing — and the third reading of the by-law does not take place until the Ontario Municipal Board (OMB) has authorized the debenture issue. Tenders or quotations from bond dealers may be required by the municipality’s procedure by-law or by custom (see page 14). If so, they are obtained before the third reading so that the actual terms of sale incorporated in the dealer’s contract may be specified in the by-law. Before

debentures are sold, the by-law is either validated by the OMB or a legal counsel (who is an acknowledged authority on municipal law) provides a written opinion on its validity. The “validation” is printed on the back of the debenture certificates.

The OMB issues an official board “Order” to approve a debenture issue, or to confirm any tentative approval which may have been given earlier. This Order is signed and sealed. It sets out such details as: the project cost, the amount and term of the debenture issue, and permission for temporary financing pending the sale of debentures. Firm arrangements are made for either selling the debenture issue or for temporary bank financing before the OMB gives its final approval.

The minimum procedures which are followed to obtain long-term financing from the provincial government or CMHC vary from program to program. In general, it is essential to obtain the approval of the agency responsible for administering the relevant grant or loan program before a capital project is begun.

Your client will experience serious financial and legal difficulties if it fails to follow these minimum procedures when obtaining long-term financing. For example, the OMB is unable to approve long-term financing for a project which has already started. The municipality is then in the embarrassing position of having to finance an unapproved project from current revenues or of obtaining

a private act of the Legislature to approve long-term financing. If legal counsel will not give a favourable opinion on a debenture by-law or if the OMB cannot validate it, a dealer may break his commitment to purchase the debenture issue. Furthermore, after a technically illegal project is begun or well advanced, a ratepayer may initiate court action to frustrate it.

Incidentally, the requirements of *The Securities Act* do not apply to an offering of municipal debentures to the public; so you are not required to take an active part in preparing a prospectus when your client is seeking long-term financing.

Long-term financing — internal procedures

Most municipalities find a long-term capital budget indispensable for management purposes. This budget is prepared by the treasurer in close consultation with the appointed department heads who are responsible for actually spending the money. It shows all proposed capital expenditure, all the proposed sources of financing and the anticipated effects upon the current revenues and expenditures for at least the next five years. The long-term capital budget is reviewed and updated by the council every year.

The five year forecast of proposed long-term borrowing — which the OMB requires annually from many municipalities — is compiled from this long-term capital budget. The inclusion

of a project in the forecast does not constitute a formal application for approval of the project — but if the OMB accepts the forecast for the current year, the only OMB approval required is for the issue of debentures.

Capital expenditure — internal procedures

In addition to the long-term capital budget, a detailed capital budget is developed for the current year, in order to provide control over capital expenditure in that period. Cost and financing records are kept for each project so that actual costs can be compared with the estimated costs and the contract terms. If at any time during a project, the actual costs are exceeding either the anticipated costs or the amount that the OMB or any government agency has authorized, the deviations should be reported so that the appropriate official or the council may take prompt corrective action.

The council passes a by-law approving the project and its financing. Tenders for capital projects are called in accordance with the procedure by-law or the established practice of the municipality.

The advice of the municipal solicitor on any proposed contract should be obtained before the council signs and seals it.

An adequate amount of performance bonds or cash deposits, together

with liability insurance, should be obtained from the contractor for each project.

Summary of documentation

Once you become familiar with the preliminary legal requirements and internal administrative procedures relating to a capital project, you should have no difficulty in deciding on the documentary evidence you will want to examine during your audit. The documents generally available for your examination include:

- a by-law approving any long-term borrowing
- a bond dealer's contract for a debenture issue
- an OMB Order approving any long-term borrowing
- approval from the appropriate government department or agency of any project for which grants or loans are anticipated
- the long-term capital budget
- a by-law approving the project
- tenders for construction (if required by the procedure by-law)
- the construction or purchase contract, showing all details and terms
- appropriate project records showing costs and financing.

Capital projects subject to specific statutory controls

In certain types of projects, the legal requirements and controls are rigorous. There are three good reasons why. First, project costs have to be assessed against certain ratepayers in an equitable way; second, provincial and federal grants may be involved in the finance of the project; third, previous lack of control has resulted in costly mistakes.

Subdivision development

Municipalities have extensive authority under *The Planning Act* to plan, zone, control and regulate the subdivision of land for residential or commercial purposes. Using this authority, a municipality both plans and controls its own development and also obtains contributions from subdividers toward the cost of installing services to the subdivisions.

When a subdivision is envisaged in a municipality, there is often a wide difference of opinion about the development, its rate of progress and method of financing. The developer, who bears the financial risk, naturally wishes to have his plans approved promptly and to avoid any additional financing burden. On the other hand, the local planning board and the council have to consider the long-term effects of the development and the available sources of funds for installing necessary municipal services. Rapid development on a sound financial basis can take place only if strong leadership, prudent procedures and

competent professional advice are present in the municipal administration.

Since subdivision development control is primarily a local concern, there is no uniform procedure for all municipalities. However, a complete program for planning, zoning and controlling subdivisions usually takes this form:

- i. The local planning board prepares a land-use plan. This plan, when it has been approved by the council and the Community Planning Branch of the Department of Municipal Affairs becomes the Official Plan. Where there is an Official Plan, the municipality's zoning by-laws and subdivision control ensure that all improvements and developments conform to it, although a committee of adjustment may authorize minor changes in both the Official Plan and the zoning by-laws.
- ii. The municipal council passes zoning by-laws to control both land use and development. The OMB must approve all zoning by-laws, and any amendments to them.
- iii. The municipal council may designate an area "subject to subdivision control". In so doing, it obligates subdividers to submit their plans to the Community Planning Branch of the DMA. This Branch generally lays down certain conditions before it will approve a subdivision plan: they include a requirement that the subdivider install at least minimum municipal services (such as paved streets, sewage,

water supply, etc.) and that the plan fits in with other factors affecting the development of the area — such as new highway construction, projected sewage treatment plants, railway extensions and so on.

- iv. After the subdivision plan has been approved, the subdivider enters into an agreement with the municipality. In this subdivision agreement, the services to be installed are set out together with details concerning related financial arrangements.

As a matter of practical administration, the agreement is often drawn up by the planning board (who should have competent professional advice from financial, legal, planning and engineering specialists). The council provides its final approval by passing a by-law.

A municipality may receive large sums of money from a subdivider under the terms of a subdivision agreement. Most of it is for capital expenditure and is held in a reserve fund until it is used (see *Bulletin 4 of the Municipal Finance Manual*, page 404). As auditor, you should determine whether the internal control and accounting systems are adequate enough to ensure that subdivision development money is used for the specific purpose for which it was acquired and that excess money is returned to the subdivider. If money has been received which is to be used for general services necessitated by the subdivision of land, these services are understood to include the provision of sewage treatment facilities, com-

munity centres, parks and other indirectly related capital projects which may not be located geographically within the subdivision. Money received from a subdivider for engineering services to be provided by the municipality is treated differently from the other money paid by a subdivider; it is earmarked to meet engineering costs as they are incurred (see “netting of expenditure”, page 202 of *Bulletin 2, Municipal Finance Manual*).

Your client may retain you as its financial advisor, as well as its auditor, so you should be aware of the effect of the terms of a subdivision agreement on your client’s cash position. If your client has to make major expenditures on the subdivision before it receives contributions from a subdivider, the cost of financing these expenditures will have to be met out of general tax revenues. You should also be aware that if your client fails to require a subdivider to pay the full cost of installing municipal services, the municipality will have to finance the capital cost of these services, possibly through local improvement charges.

Local improvements

The Local Improvement Act authorizes municipalities to install services such as sewers, drains, water mains, street-lighting and sidewalks, and to recover the costs from benefitting land-owners. These services are usually financed by issuing debentures and recovering the debt charges from land-owners over a period of years. Sewers and water mains can also

be supplied in a similar way under the provisions of *The Municipal Act*.

Local improvements entail statutory requirements concerning OMB approval, the apportionment of cost and the appealing of assessments:

- i. For capital projects under *The Local Improvement Act*, approval of the OMB is obtained for the project, if it was initiated by the municipal council, or if it was initiated by a petition of land-owners and there were objections to it. The municipal treasurer prepares a special report which apportions the cost of the project among the land-owners affected, in accordance with *The Local Improvement Act*. These land-owners have the right to appeal the apportionment to the municipality's court of revision when it meets to review the treasurer's report.
- ii. For capital projects under *The Municipal Act*, OMB approval is required for the construction of the project and for the by-law which imposes a special charge on the affected land-owners (or occupants) in order to recover the cost of the project. Objections are heard by the OMB before it approves the by-law, but there is no appeal of the assessment.

The documents you may expect to find available for examination include in the case of a project carried out under *The Local Improvement Act*:

- the original by-law authorizing the project with the OMB's required approval
- the treasurer's report of costs and his apportionment of costs, passed by the court of revision
- the local improvement assessment roll
- the council's minute adopting the local improvement assessment roll.

in the case of projects under *The Municipal Act*:

- the by-law authorizing the project and imposing a special rate to recover its cost, with the OMB's required approval.

Projects under The Drainage Act

The provincial government subsidizes the cost of draining farm land, if the drainage project is carried out under the provisions of *The Drainage Act*. There are statutory requirements for apportioning costs, appealing assessments, and claiming a grant:

- projects are initiated by a petition from land-owners. An engineer is then appointed to report on the drainage requirements of the area, the cost of meeting them, and the apportionment of costs to each benefitting land-owner
- land-owners affected must be notified of the proposed project, so that they may be heard at a meeting where the project is considered.

They may appeal the technical requirements to a referee, and their assessed portion of the estimated cost to the municipality's court of revision

- the municipal council passes a by-law authorizing the drainage project and the basis of assessing costs against the benefitting land-owners. To be eligible for a grant, a "Notice of Intent" must be filed with the Municipal Subsidies Branch of the DMA before the project is actually started.

The documents you may expect to examine include:

- the engineer's report showing the estimated costs and their apportionment
- the minutes of the court of revision
- the municipal by-law and special assessment roll
- the correspondence from the DMA concerning the grant.

Ontario Water Resources Commission

The Ontario Water Resources Commission (OWRC) is an agency of the provincial government charged with controlling the standard of — and in some cases providing — water supply and sewage treatment services in Ontario. If requested, the OWRC provides these services for a municipality and charges it with the cost.

Where a municipality carries out its own sewage treatment or water

supply project, the approval of the OWRC is required. Where the OWRC carries out the project, the municipality is relieved of the detailed administration and accounting relating to it. See the *Municipal Finance Manual, Bulletin 3*, pages 305 and 306, which details the types of agreement that can be made with the OWRC for a project.

Urban renewal

Urban renewal projects change the character and appearance of important parts of a municipality. The statutory requirements and administrative procedures affecting these projects are onerous because municipal, provincial and federal governments as well as private developers are involved in urban renewal.

In order that an urban renewal program can proceed in an orderly and economic manner, a high degree of planning and organization is necessary. The use of budgets and cash forecasts is essential for good program management. Full details of costs and financing should be reflected for each phase of the project.

The documents you may expect to examine include:

- a municipal by-law which designates the area for redevelopment, and which has received the approval of the Community Planning Branch of the Department of Municipal Affairs
- a redevelopment plan approved by the local planning board, and a

municipal by-law approving the plan, with the OMB's required approval

- an OMB Order approving the cost and financing arrangements for the project
- agreements with the province and with CMHC, reflecting all the detailed subsidy arrangements.

The capital project in process

You might find it helpful if we reviewed a “typical” project through its stages of construction and financing. Bear in mind that not all the steps outlined here are pertinent to all capital projects. For example, where vehicles are being purchased or where a road widening is not being financed by debentures, some of these steps do not apply.

Temporary capital financing

Usually, the initial stages of a project are financed by temporary borrowing. Money may not be borrowed on a temporary basis until after the council has passed a by-law authorizing the project. Banks generally require a certified copy of this by-law with an application for a temporary loan, sometimes with a copy of the OMB order for the project.

Temporary borrowing for capital purposes is limited by statute to the amounts specified in the OMB order, plus any additional amounts the OMB may approve. Temporary funds

obtained for capital projects may be used only for those projects and for no other purpose; they are repaid when the project is permanently financed — either from the proceeds of the debenture issue, or from the relevant government grant, or from the revenue fund.

Contract payments

All progress payments are made in accordance with the contract authorized by the council. The project is inspected by the municipal engineer — or by a consulting engineer or architect — who then certifies the payment request from the contractor before it is paid. Any payments which are for “extras”, or in excess of the contract agreed to by council, are approved by the council before payment is made. Payment of the holdback after the completion of the project is also approved by the council, as this payment can release the contractor from further obligations.

Subsidies

As an auditor you may be involved in the procedure for claiming subsidy payments from different departments of the provincial government. Procedures for paying subsidies vary from program to program, and the accounting criteria by which provincial departments distinguish between capital and non-capital projects may not coincide with your client's accounting principles.

It is possible to confirm directly with the appropriate provincial government

department the amount of subsidy paid to a municipality during the year. The address of the proper government officer to write to for each subsidy is in your *Municipal Finance Manual*.

Control of debentures and coupons

Rigorous control should be maintained over debentures and coupons.

Once debentures have been signed by the head of the council and the treasurer and have been sealed, care must be taken during their delivery to the purchaser or broker. If they are sold “over the counter”, serially numbered receipts are used to provide further control.

A bank is authorized to handle cashing of coupons, and when debentures mature, they are also surrendered to the authorized bank for payment. The debenture register is used by the municipal treasurer to maintain accounting control over cashed coupons and debentures. A system should exist at the bank to cancel cashed coupons and matured debentures before they are delivered to the municipality.

When debentures are issued by one municipality and the liability is assumed by another, the basis of assumption is established by an OMB order, by legislation, or by an agreement between the two municipalities concerned.

Excess debenture proceeds

You should know the legal limitations

on the use of debenture proceeds which are in excess of the cost of the project for which they were issued. Any excess funds realized from a sale of debentures may be applied only:

- to redeem one or more debentures of the latest maturity, where the amount of the excess is sufficient and the debentures are so redeemable
- to the annual payments of principal and interest on the debentures until the excess has all been applied
- to buy back the debentures
- with the approval of the OMB, to meet other capital expenditure which would otherwise have been met from taxation upon the same class of ratepayers as bear the debt charges on the debenture issue which gave rise to the excess proceeds.

Contributions to capital expenditure

A council by-law should be available for your examination to support a contribution to capital expenditure from the revenue fund, from reserve funds, or from reserves. Where a contribution is from a reserve, the total amount transferred in the year may not exceed the restriction imposed by the Department of Municipal Affairs (see page 405 in *Bulletin 4* of the *Municipal Finance Manual*). Where the capital expenditure is for a purpose different from that of the reserve fund,

the approval of the Department is required for each transfer from the fund.

Disclosing material commitments

You should realize the practical problem involved in providing full and clear disclosure of all material commitments at the balance sheet date. A long time may elapse during the planning of capital projects, the obtaining of the council's agreement, the completion of the preliminary legal steps and the obtaining of permanent financing. As a result, there may be a lot of confusion about just when your client is actually committed to make capital expenditures, as well as the actual amount of its contractual obligations. Nevertheless, as recommended in the *CICA Handbook*, all contractual obligations and commitments for capital expenditure that are abnormally large in relation to the usual operations of the municipality should be reported in a note to the financial statements. The note should also disclose the proposed financing of the projects, so that it indicates clearly the effect debt will have on the financial position or future operations of the municipality.

The capital project after completion

Fixed assets are not reported on a municipality's balance sheet, and the accounting records related to fixed

assets may be minimal. Nevertheless, there are extensive management records related to fixed assets. These records provide for the efficient maintenance, insurance and use of assets, as well as adequate safeguards to prevent their unauthorized disposal. *Bulletin 5 of the Municipal Finance Manual* describes the types of records which are usually kept.

In your evaluation of your client's internal control, you may want to examine the system of record-keeping for fixed assets, and also to advise your client concerning the control over fixed assets.

The sale, disposal or abandonment of assets should be authorized by the council. Procedures vary, depending upon the municipality's procedure by-law; however, it is often considered worth the cost to have an independent appraiser value an asset before sale. Or tenders may be called for the sale of assets by the municipality.

The Municipal Act restricts the use of proceeds from the sale of assets on which there is still debt outstanding. The restrictions are the same as those applied to the use of excess debenture proceeds (see page 55). If the asset is free of debenture debt, the use of the proceeds is at the discretion of the council. It is good general practice for a municipality to regard the disposal of an asset as a source of capital funds to be used to finance further capital expenditure.

OTHER AREAS

Temporary borrowing, fidelity insurance and reserve funds and other special funds have unusual statutory requirements.

Temporary borrowing

There are stringent statutory limitations on the use of *temporary* borrowing by a municipality. Every loan made to a municipality is authorized by a by-law and secured by a promissory note. A municipality has no authority to incur a bank overdraft or any other unsecured loan.

Loans are made for current operations or for capital purposes. Loans to finance current municipal operations are limited to 70 per cent of estimated uncollected revenues for the year; if it is necessary to exceed this limit, the approval of the OMB must be obtained. “Estimated uncollected revenues” refers to the anticipated income of the revenue fund from all sources, including taxes for the year and revenue contributions from other governments.

At the same time as the OMB gives a municipality permission to undertake long-term borrowing, it approves temporary financing up to the cost of the project (see page 48).

Temporary loans for current purposes are repaid out of the current or preceding year’s revenues when they are received. Proceeds from the sale of debentures must be used to repay temporary loans for capital purposes. These terms are written into a standard form of by-law which is provided by banks.

A temporary loan is a liability of the fund indicated in the authorizing by-law. For example, a by-law is passed in which a capital fund loan is inadvertently authorized on a revenue fund by-law, it is a liability of the revenue fund and is reported as such. This type of mistake should be avoided because it can result in restrictions to future borrowing; it also confuses the source of funds from which a loan is to be repaid.

In order to determine adherence to statutory limitations you should know the balance of each capital loan, and the balance of the temporary loans for current operations. You will also need to ensure the separation of capital from current loans in the financial statements. Banks provide these details on a standard bank confirmation form.

Few local boards have the legal authority to incur their own debt; in most cases the municipality must borrow on their behalf. You should ask the appropriate official for his authority for any direct loans to a local board.

Fidelity insurance

The law requires a municipality to bond its treasurer, deputy treasurer, collector and any other officer designated by the council, and the council to review the adequacy of its bond coverage each year.

In practice, coverage has frequently proved inadequate — reflecting a short-sighted attitude towards obtaining insurance. An effort to save a few dollars may result in irrecoverable losses.

Encourage the council to provide blanket insurance in adequate amounts on all its employees and additional insurance for positions of greater responsibility.

Reserve funds and other special funds

Reserve funds are resources segregated to pay for costs to be incurred

at a future date. Other special funds include trust funds, pension funds and sinking funds. Full details of these funds — plus the statutory limitations for establishing investing and spending these funds — are to be found in your *Municipal Finance Manual* on pages 403-405. You should review this information before you start this part of your audit.

The law requires that earnings of a fund's assets become the property of the fund and that they must be used for the same purpose as the fund. The legislation and by-laws affecting each fund indicates where special features of control may be necessary.

POSTSCRIPT

If you have found this book interesting, stimulating and helpful, it has served its purpose. It makes no pretence at being the last word on municipal auditing and we hope you will forgive any omissions you may have found. By all means use the checklists on pages 60-62. They are no substitute for reading the book as a whole, but they provide you with a handy memory aid. Use them as you review your municipal client's systems.

Once you have explored the complexities of municipal auditing you will want to obtain a greater depth of theoretical understanding than is possible in a book of this nature: that is why we have included a fairly broad bibliography. At the same time, there are problems about auditing a number of other areas of local government each of which would require a book of its own to cover adequately — local boards and boards of education are but two examples. We hope more books can be issued in the not too distant future, but in the meantime, you will have to do some digging for yourself. Members of our Department are only

too glad to answer any questions you may have on local government.

Local government and public accounting are two facets of modern life that are changing with startling rapidity. So we expect this book to become obsolescent within a short space of time; do not rely on it slavishly. Treat it as a guide only — and check on the latest legislation and Institute standards before you proceed to audit a municipal client.

Municipal operations involve vast sums of money. Their planning and financing can have a profound effect not only on the present municipal inhabitants but also those of tomorrow. So your audit should surely involve much more than a detailed check of approvals, initials and signatures; take every opportunity to step back and consider how the current actions of your client will affect the future. By counselling your client towards sound and progressive policies you could be rendering him your greatest audit service. Always perform your evaluation of the municipal systems with this precept in mind.

MUNICIPAL AUDIT REMINDER LISTS

Introduction

These lists are designed to help you make a comprehensive review of municipal systems. They review the contents of the chapters covering revenue, expenditure, capital and other areas.

The controls outlined in these lists are those found in a well administered municipality. You should consider them to be a yardstick against which to measure your client’s systems — not as absolute requirements.

Revenue (Pages 34-41.)

1. Does the council pass by-laws establishing policies for:

- (a) Allocation of responsibilities for collecting and controlling revenue?
- (b) Tax instalment dates?
- (c) Interim tax billing?
- (d) Collecting taxes?
- (e) Joint municipal agreements?
- (f) Fee schedules?
- (g) Approval of annual estimates and mill rates?

2. Do appointed officials have established procedures for:

- (a) Reviewing the assessment roll?
- (b) Appealing assessments where necessary?
- (c) Correcting and updating the assessment and collector’s rolls?
- (d) Preparing the budget tax rate by-law?

(e) Preparing tax bills and tax revenue summary — including the addition of special charges and amounts added for collection?

- (f) Billing and collecting supplementary taxes?
- (g) Collecting business taxes?
- (h) Tax sales or tax registrations?
- (i) Billing and collecting penalties and interest on overdue taxes?
- (j) Claiming, checking and recording payments from other governments?
- (k) Recovering federal and provincial sales tax?
- (l) Controlling revenues from licences, permits and fees?

3. Are budgets adequate enough to:

- (a) Identify the source of all expected revenue?
- (b) Identify surplus funds available for temporary investment?

4. Do financial reports provide the information necessary for the control of collections?

5. Have the legal requirements of the provincial statutes been observed for:

- (a) Updating and correcting the assessment and collector's rolls?
- (b) Preparing the budget and tax rate by-law?
- (c) Preparing and distributing tax bills?
- (d) Collecting taxes?
- (e) Charging penalties and interest on overdue taxes?
- (f) Tax sales or tax registrations?
- (g) Billing and collecting supplementary taxes?
- (h) Joint agreements with other municipalities?
- (i) Imposing charges for other revenue?

Expenditure (Pages 42-46.)

1. Does the council pass by-laws establishing policies for:

- (a) Allocation of responsibilities for controlling expenditure?
- (b) Annual expenditure estimates?
- (c) Limits for purchase approvals?
- (d) Purchasing and tendering?
- (e) Payment of accounts?

(f) Personnel and wage rates?

(g) Insurance coverage?

2. Do appointed officials have established procedures for:

- (a) Purchasing and tendering?
- (b) Payment of accounts?
- (c) Preparation of annual estimates?
- (d) Hiring and payroll preparation?
- (e) Control of inventories?
- (f) Preparation and distribution of internal financial reports?

3. Do department heads initiate adequate departmental procedures for:

- (a) Requisitioning?
- (b) Purchasing?
- (c) Receiving?
- (d) Storage?
- (e) Approval of payments?

4. Do the budgets identify expenditure limits by control centre?

5. Do the financial reports provide the information necessary to manage each control centre?

6. Have the legal requirements of the provincial statutes been observed for:

- (a) Amounts to be paid to bodies for which the municipality must

raise taxes; boards of education, counties, etc.?

(b) Amounts raised for special area charges: police villages, service areas, etc.?

(c) Transactions involving reserves?

(d) Taxes written off?

(e) Deficits?

(f) Contributions, grants and subsidies?

(g) Obtain performance bonds and liability insurance?

(h) Control cashed debenture coupons?

(i) Control and insure fixed assets?

(j) Dispose of fixed assets?

3. Do the financial statements properly reflect:

(a) Capital expenditure regardless of how financed?

(b) Long term liabilities?

(c) Capital outlay to be recovered in future years?

(d) Contractual obligations and contingent liabilities?

Capital (Pages 47-56.)

1. Have the legal requirements been observed for:

(a) Obtaining OMB approval?

(b) The use of money received from subdividers?

(c) Apportioning costs of projects not financed from general revenue?

2. Are there adequate procedures to:

(a) Prepare a capital budget?

(b) Document each project?

(c) Control costs of each project?

(d) Correct unfavourable trends in costs?

(e) Call tenders?

(f) Obtain professional advice when needed?

Other areas (Pages 57-58.)

1. Have the legal requirements of the provincial statutes been observed for:

(a) Temporary loans for current operations?

(b) Temporary loans for capital purposes?

(c) Fidelity insurance coverage?

(d) Reserve funds and other special funds?

2. Is there adequate fidelity insurance coverage?

ASSESSMENT APPEAL PROCEDURE

APPEAL MAY BE MADE TO	WITHIN THE FOLLOWING PERIOD	BY THESE ELIGIBLE PARTIES	FOR THESE REASONS
ASSESSMENT COMMISSIONER	Between the delivery of the assessment notices to the rate-payers and the assessment roll to the municipal clerk — at least 15 days	Any person	Any information on the Assessment Roll
ASSESSMENT REVIEW COURT	14 days after the delivery of the Assessment Roll to the municipal clerk	Any person including a municipality or a school board	(a) Any error or omission in regard to himself (b) That the assessment of his or any other person is too high or too low
COUNTY COURT JUDGE	14 days after notice of decision of the assessment review court has been given by the regional registrar	A municipal corporation, a school board, assessment commissioner, any person assessed or any municipal elector of the municipality	(a) The decision of the Assessment Review Court (b) The omission, neglect or refusal of that court to hear or decide an appeal
ONTARIO MUNICIPAL BOARD	21 days after the mailing of the notice of the decision of the county court judge	The municipal corporation, a school board, the assessment commissioner, any person assessed and any person who has filed a complaint with the Assessment Review Court in that year	(a) The decision of the county court judge (b) The decision of the Assessment Review Court for assessments over \$50,000
COURT OF APPEAL	15 days after the delivery of the order of the OMB	The same people who could appeal to the OMB	The decision of the OMB upon all questions of law or the construction of a statute, a municipal by-law, any agreement in writing to which the municipality concerned is a party, or any order of the Ontario Municipal Board

NOTE: There is the same time-table for people assessed subsequent to the closing of the Assessment Roll. Any person involved should review the appropriate legislation.

BIBLIOGRAPHY

This listing of books and periodicals is by no means exhaustive; neither does it consist of required reading for municipal auditors. Some of the titles you may want to have in your office for reading and frequent reference — others you may never read unless you have a particular interest in a special aspect of municipal practice.

Rather than give you a massive listing of books and papers — which might look impressive but is often totally unhelpful — we have carefully selected those titles we are sure will be of most use to you. We have added our own subjective comments to help you decide whether or not you want to purchase or borrow a particular book or periodical. It may well be that we have missed a useful title or two. If you come across a book or paper which you feel would be of help to other municipal auditors, please let us know so that we can pass on the information.

Accounting

1. Municipal Finance Officers Association of the United States and Canada. *Government Accounting, Auditing and Financial Reporting*. Chicago: 1968. 234 pages.

An authoritative reference describing North American practice, not entirely pertinent to practice in Ontario.

2. Ontario, Department of Municipal Affairs, *Municipal Finance Manual*, Toronto, (\$5.00).

A loose-leaf binder which contains *Bulletins* explaining accounting principles and practices (if they differ from business practice) and detailed instructions for completing the annual financial statements of municipalities. Regularly updated.

Auditing

1. The Canadian Institute of Chartered Accountants Study Group on Audit Techniques,

a. *Confirmation of Accounts Receivable*. 1969. 31 pages

b. *Internal Control and Procedural Audit Tests*. 1968. 38 pages

c. *Internal Control in the Small Business*. 1967. 31 pages

d. *Materiality in Auditing*. 1965. 22 pages.

Well-researched technical studies containing many ideas that are applicable to municipal auditing and that have been accepted as good general practice. Available from the CICA offices in Toronto.

2. The Institute of Internal Auditors, *Sampling Manual for Auditors*. New York. 1967. 120 pages.

A working handbook on the application of sampling techniques by auditors. Not exhaustive but it does provide the reader with the principal uses of sampling and some statistical tables.

3. Skinner, R. M. and Anderson, R. J.,

Analytical Auditing. Toronto: Sir Isaac Pitman (Canada) Limited, 1966.
163 pages.

A basic reference text which describes one approach to the evaluation of internal control.

Budgeting

- 1. Moak, L. L. and Gordon, K. K.,
Budgeting for Smaller Governmental Units: Chicago. Municipal Finance Officers of United States and Canada, 1965. 194 pages.

Covers the problems and actual experiences of budgeting in 20 smaller cities (population 12,000 to 70,000).

- 2. Moak, L. L. and Killian, K. W.,
Capital Programing and Capital Budgeting. Chicago: Municipal Finance Officers of the United States and Canada, 1964. 152 pages.

Describes the need for separation of the capital program and the capital budget and the procedure involved in preparing both. Also includes studies of the use of these instruments in 17 cities with suggestions for desirable practice in each case.

- 3. Moak, L. L. and Killian, K. W.,
Operating Budget Manual. Chicago: Municipal Finance Officers of the United States and Canada 1963.
347 pages.

Part of a series on budgets in municipal government. Includes guidelines for the preparation, consideration, adoption and administration of operating budgets in larger municipalites.

Finance

- 1. The Canadian Institute of Chartered Accountants, *Municipal Finance and Administration in Canada*. Toronto: 1967. 54 pages.

Reprints of 10 articles from the *Canadian Chartered Accountant*. Some of the information does not apply to Ontario.

- 2. *Canadian Public Administration*.

A quarterly journal reflecting the scholarly research of university teachers in public administration, and the practical experience of senior civil servants. Most issues contain at least one article which is relevant to local government finance or administration. Available from The Institute of Public Administration of Canada, 45 Broad-albane Street, Toronto 189, Ontario.

- 3. Canadian Tax Foundation, *Local Finance*, Toronto: (open series).

A series to date of 23 studies and reports on municipal finance and taxation containing comparative financial statistics, supplemented by narrative interpretation and explanation. Subjects include public health and welfare, community planning, pollution control and regional government throughout Canada.

- 4. *Canadian Tax Journal*

A bi-monthly journal which sometimes contains excellent articles on local government finance, particularly in the areas of assessment and taxation. Available from the Canadian Tax Foundation, 100 University Avenue, Toronto 116, Ontario.

5. Dupre, J. S., *Intergovernmental Finance in Ontario — a Provincial Local Perspective*. Toronto: Queen's Printer. 142 pages.

A background paper to the report of the *Ontario Committee on Taxation*. It describes the provincial-municipal financial relationships in detail and with great clarity, as well as providing valuable historical background to the development of the existing chaotic grant system.

6. The International City Managers Association, *Municipal Finance Administration* (6th edition). Chicago: Institute for Training in Municipal Administration, 1962. 519 pages.

Written as a guide to help senior appointed officials improve the administration of services within their municipality.

7. Macauley, R. W., *The Report of the Smith Committee on Taxation: A Synopsis*. Don Mills: CCH Canadian Limited, 1968. 234 pages.

A summary of all the recommendations of the *Ontario Committee on Taxation* including a synopsis of the reasons for each recommendation and its predicted effects.

8. Marshall, A. H., *Financial Administration in Local Government*; Royal Institute of Public Administration. Toronto: University of Toronto Press, 1960. 385 pages.

A basic reference text describing present-day municipal finance practice in municipalities in England. Most of the ideas are also applicable to Ontario

because of the similarities of local government organization and finance.

9. Ontario, *The Ontario Committee on Taxation*, (The Smith Report) 1967. Toronto: Queen's Printer, 1967. 3 volumes: 343 pages, 549 pages and 473 pages.

Volume II contains the best available description of local government taxation and finance in Ontario. Some parts are already dated by changes since publication, but it contains a great deal of well-written information based on reliable, detailed research.

General

1. Crawford, K. G., *Canadian Municipal Government*. Toronto: University of Toronto Press, 1954. 407 pages.

The standard text on the organization and finance of local government across Canada, with specific information about each province. Although much of the detailed information is now dated, it provides reliable background reading.

2. *The Municipal World*

A monthly journal which contains up-to-date information on the activities of municipal associations, changes in legislation and practices that affect municipalities, the changing provincial-municipal relationship, and reflections on current government policies. Write: The Municipal World Ltd., Box 399, St. Thomas, Ontario.

3. Ontario, Department of Municipal Affairs, *Municipal Directory*, Toronto: annually. (\$1.00).

A listing of municipalities by county or district with population, assessment, telephone number, and the name and address of each head of council, chief administrative officer, clerk, treasurer and engineer or road superintendent. Names and telephone numbers of officers at the D.M.A. are also included.

4. Ontario, Department of Municipal Affairs, *Provincial Assistance to Municipalities, Boards and Commissions*. Toronto. (\$2.00)

A loose-leaf binder which provides information about the major active provincial grant programs. Its contents are updated regularly.

5. Ontario, Department of Municipal Affairs, *Summary of Financial Reports of Municipalities*, Toronto: annually. (5.00).

Provides summary of the financial reports of all Ontario municipalities. Helpful in compiling comparative statistics.

6. Ontario, Department of Municipal Affairs, *Summary of Legislation affecting municipalities*. Toronto: annually.

Supplied at no charge to municipal auditors when published.

7. Ontario, *The Ontario Gazette*. Toronto: Queen's Printer, weekly.

Contains information about regulations, tax sales, royal assent to bills, and proclamation of acts in Ontario.

8. The Ontario Municipal Association, *The Municipal Council and Councillor*

in Ontario. Toronto: 1966. 67 pages.

A readable, concise introduction to the organization and accountability pattern in Ontario Municipalities, written from the viewpoint of a newly elected member of the council.

Law

1. Association of Municipal Clerks and Treasurers of Ontario. *Where to Find the Law*. Toronto: 1967. 18 pages.

Useful, up-to-date, concise instructions and suggestions, explaining time-saving procedures to the average municipal administrator.

2. MacTavish, L. R., *The Ontario Statute Citator*.

A reliable, time-saving updating service to the *Revised Statutes of Ontario*. It incorporates all legislation once it has become law. Write: Canada Law Book Limited, 100 Richmond Street East, Toronto 210, Ontario.

3. Ontario, *Revised Statutes of Ontario 1960*. Toronto: Queen's Printer.

RSO contain the consolidation of the public general acts of the legislature of Ontario. Next edition will be updated to August 1, 1970. Annual *Statutes of Ontario* contain the Public and Private Acts passed at each session.

4. Rogers, I. M., *The Law of Canadian Municipal Corporations*. Toronto: The Carswell Company Ltd., 1959. 2 volumes.

The basic text on current municipal law. Updated by occasional supplements. Co-ordinates various statutes and

explains their interpretation by the courts.

Tax Collections

1. Association of Municipal Clerks and Treasurers of Ontario, *Licensing and Trade Regulation*, Toronto: 1967. 31 pages.

General background and rationale for municipal licensing powers. A good review of a complicated subject.

2. The Municipal World, *Tax Arrears Procedures and The Department of Municipal Affairs Act*. St. Thomas, Ontario: 1965. 27 pages.

Extracts from the statutes and regulations explaining the necessary steps under the tax registration procedures.

3. The Municipal World, *Tax Sale Procedure under The Assessment Act*. St. Thomas, Ontario: 1964. 37 pages.

Extracts from the statutes and regulations explaining the necessary steps under the tax sale procedures. Statutory references are now outdated because the relevant sections have been transferred to *The Municipal Act*.

Statutes

The Assessment Act

The Cemeteries Act

The Community Centres Act

The Department of Municipal Affairs Act

The Drainage Act

The Highway Improvement Act

The Local Improvement Act

The Municipal Act

The Ontario Water Resources Act

The Ontario Municipal Board Act

The Planning Act

The Power Commission Act

The Public Libraries Act

The Public Parks Act

The Public Utilities Act

The Tile Drainage Act

Toronto: Queen's Printer.

These are the statutes which you most likely need to have available for day-to-day use. Others, such as private acts and statutes which apply only to a specific municipality or region, are not included.

Note: All statutes and publications of the Ontario Government are available through the Ontario Government Book Store, 880 Bay Street, Toronto 181, Ontario. Cash must accompany the order.

